



The State Bar *of California*

OPEN SESSION

AGENDA ITEM

JULY 2019

PROGRAMS COMMITTEE III.A

DATE: July 30, 2019

TO: Members, Programs Committee

FROM: Hellen Hong, Director, Office of Access & Inclusion

SUBJECT: Approval of Leadership Banks Program

EXECUTIVE SUMMARY

Each year the State Bar of California distributes grants to qualified nonprofit legal aid organizations providing free legal services to low-income Californians from the Interest on Lawyers' Trust Accounts (IOLTA). In order to advance the State Bar's goal of increasing access to justice, the State Bar seeks to establish a Leadership Bank Program to encourage eligible financial institutions to elect the established compliance (interest) rates for their IOLTA accounts. These Leadership Banks would be highlighted on the State Bar's website as preferred IOLTA eligible institutions because they provide increased revenue for free civil legal services.

BACKGROUND

IOLTA STATUTE

In 1981 the Legislature authorized the Interest on Lawyers' Trust Accounts (IOLTA) program under Business and Professions Code section 6210-6228 (IOLTA statute) to increase access to justice and improve the administration of justice through expansion of legal services, improving the quality of existing free legal services in civil matters to indigent persons and initiating new programs to provide such services.

The IOLTA statute requires lawyers to place client funds that are on deposit for short periods of time or of nominal amounts into interest- or dividend-bearing accounts in which the interest or dividend is paid to the State Bar. Such IOLTA accounts can only be kept at approved financial

institutions certified by the State Bar to ensure compliance with the IOLTA statute. If there is a large sum of money involved, or it will be held for a long time, an attorney should hold the client's funds in an individual account, designated as a Client Trust Account, and the interest earned will go to the client.

The interest earned from pooled IOLTA accounts is remitted to the State Bar. The State Bar subtracts its administrative costs and then distributes the approved funding amount (based on the IOLTA statutory formula) to qualified legal aid nonprofit organizations who provide free legal services in civil matters to indigent persons in California. The Office of Access & Inclusion administers the Legal Services Trust Fund Program for the State Bar under the oversight of the Legal Services Trust Fund Commission (LSTFC) and Board of Trustees.

In 2007, Assembly Bill (AB) 1723 (Jones, Ch. 422, Stats. of 2007) amended the IOLTA statute to specify that IOLTA accounts should earn no less than the interest rate or dividend generally available to non-IOLTA depositors at the same institution. This is referred to as “comparability.” However, since that change in the law became effective in 2008, interest rates plummeted and the IOLTA program, until recently, did not reap the anticipated benefits of comparability.

DISCUSSION

For the past two years the Office of Access & Inclusion has focused on re-certifying approximately 175 financial institutions offering IOLTA accounts to ensure their compliance with the IOLTA statute, particularly ensuring that IOLTA accounts are receiving comparable interest rates to similarly situated accounts. As a result, in 2019, the State Bar distributed \$27.6 million in IOLTA grants, nearly double the amount distributed in the prior year. The recent increase in IOLTA revenue is largely the result of rising interest rates and the State Bar’s efforts to ensure compliance with the statutory requirements.

The chart below illustrates the changes in IOLTA grant distributions over the past five years.

Year	IOLTA Grant Distribution (in millions)	Percent Change over Previous Year
2020	\$55.6 (proposed)	102%
2019	\$27.6	97%
2018	\$14	26%
2017	\$9.1	(18%)
2016	\$11.1	10%
2015	\$10	5%

The current Federal Funds Rate is within a range of 2.25 and 2.50 percent. However, it has been widely reported that the Federal Reserve may decrease the current Federal Funds Rate in 2019. A decrease in the Federal Funds Rate would likely decrease the IOLTA revenue available for the 2021 calendar year.

IOLTA LEADERSHIP BANK PLAN

Historical Context

In 2008, the State Bar adopted revisions to the State Bar Rules to reflect the comparability law codified in AB 172, mandating that IOLTA-eligible institutions pay comparable interest rates or dividends on their IOLTA accounts in one of three ways:

1. Establish IOLTA accounts as comparable-rate products;
2. Pay the comparable-product rate on IOLTA deposits accounts, less chargeable fees, if any; or
3. Pay the Established Compliance Rate (known as ECR) determined by the Legal Services Trust Fund Commission. (See State Bar Rule 2.130.)

The Legal Services Trust Fund Commission set the Established Compliance Rate at 68 percent of the Federal Funds Rate (FFR) in 2008.

However, in 2008, the nation was in the midst of the great recession and the Federal Funds Rate was 0.25 percent - the lowest possible rate. This FFR was not increased until December 2015 to 0.50 percent. For the past two years, the FFR has steadily been increasing. The chart below summarizes the relationship between the FFR and the amount of IOLTA revenue the State Bar projected for distribution for the following year to support free civil legal services.

Year	Federal Funds Rate at Year End	Approximate IOLTA Interest Revenue Distributed the following year¹ (in millions)
2015	0.50%	\$5.2
2016	0.75%	\$6.0
2017	1.50%	\$6.5
2018	2.25%	\$20.1
2019	2.50%	\$39.0

Current IOLTA Interest Rate Landscape

In California, financial institutions currently hold about \$5 billion in IOLTA deposits. For the past 18 months, the State Bar has focused on certifying nearly 200 financial institutions that hold IOLTA accounts to ensure that financial institutions are offering similar interest and dividend rates on their IOLTA products to similarly situated depositors. If these institutions are not certified they will no longer be eligible to offer IOLTA accounts to California licensees. This certification process requires individual review of each financial institution's various account products, a determination of which products are available for accounts similar to IOLTA depositors, and, if financial institutions do not elect the ECR, confirming that the rate offered for IOLTA accounts is comparable to that offered on accounts for similarly-situated depositors.

¹ Note that this differs from the total grant distributions those years, which includes contributions from licensee fees, the Justice Gap Fund and other sources.

The top 20 financial institutions with the largest deposits of IOLTA accounts hold 86 percent of the \$5 billion of deposits in California IOLTA accounts. For those top 20 financial institutions, the interest rates paid on IOLTA accounts range from 0.05 percent to 1.73 percent. In 2019, if all of the top 10 financial institutions elected to pay the ECR – currently 1.70 – that decision would yield **an increase of \$23 million** in additional funds to support free civil legal services to low-income Californians (assuming FFR remain static). The chart below highlights, for the 10 financial institutions holding the largest deposits amounts in IOLTA accounts, whether the institution has elected the ECR, and if not, the estimated average interest paid on IOLTA accounts in California, which often fluctuates based on tiered rates on sizes of deposit accounts.

Financial Institution	Average IOLTA Balances from April/May 2019 (in millions)	Percentage of IOLTA Deposits in California	ECR or Average Interest Paid on IOLTA accounts	Potential Additional Revenue for Civil Legal Services if at ECR
Wells Fargo Bank, N.A.	\$881.5	18.24%	ECR	
Bank of America	\$606.8	12.56%	ECR	
Chase Bank	\$478.4	9.90%	ECR	
City National Bank	\$430.2	8.90%	0.28%	\$6.2 million
Union Bank N.A.	\$327.2	6.77%	ECR	
Citibank	\$288.4	5.97%	0.53%	\$3.4 million
First Republic Bank	\$188.8	3.91%	0.08%	\$2.9 million
U.S. Bank	\$147.8	3.06%	1.00%	\$1.0 million
California Bank and Trust	\$129.0	2.67%	Under Certification Review	\$1.8 million
Bank of the West	\$93.8	1.94%	Under Certification Review	\$1.5 million
Total	\$3.572B	74%		\$16.8 million

Of the 160 financial institutions eligible to hold IOLTA accounts (there have been mergers since the start of the certification process), staff have only 27 remaining to review to confirm that they are providing comparable rates to their IOLTA accounts. Along with this certification process, the State Bar will be focusing on compliance; ensuring that these financial institutions continue to remit the correct interest rates on the nearly 50,000 IOLTA accounts.

Leadership Bank Proposed Program

In order to advance the State Bar's goal to increase access to justice, the State Bar is proposing a "Leadership Bank" program to encourage financial institutions to do all of the following:

1. Elect at least the ECR rate of 68 percent of the Federal Funds Rate on all accounts;
2. Waive any fees or charges on these accounts; and
3. Utilize the Bank State Bar IOLTA portal and remit payments to the State Bar.

The Leadership Bank Program would increase revenue to support civil legal services and streamline operations for the State Bar of California to monitor compliance with the IOLTA statute. These banks would be highlighted on the State Bar's website as preferred IOLTA eligible institutions because they provide increased revenue for free civil legal services. The State Bar would highlight these institutions as lead partners supporting access to justice through the IOLTA program.

The Office of General Counsel has conducted an analysis of the permissibility of such a Leadership Program and has concluded that it is permissible for the State Bar to highlight businesses that meet criteria that further government objectives. Recognizing financial institutions that pay higher interest rates, like the ECR and above, increases revenue for the State Bar Legal Services Trust Fund program, which directly advances the State Bar's statutory mission of "support[ing] greater access to...the legal system." California Business and Professions Code § 6001.1.

The State Bar plans to broadly advertise the establishment of a Leadership Bank program and provide all institutions with the opportunity to participate prior to the anticipated publication of the list in the fall of 2019.

FISCAL/PERSONNEL IMPACT

Administration of the IOLTA program is fully funded through IOLTA revenue. This recommendation does not affect the General Fund budget. No additional staff or other expenses will be incurred as a result of the adoption of recommendation.

RULE AMENDMENTS

None

BOARD BOOK AMENDMENTS

None

STRATEGIC PLAN GOALS & OBJECTIVES

Goal: 4. Support access to legal services for low-and moderate-income Californians and promote policies and programs to eliminate bias and promote an inclusive environment in the

legal system and for the public it serves, and strive to achieve a statewide attorney population that reflects the rich demographics of the state's population.

Objective: a. Support increased funding and enhanced outcome measures for Legal Services

RECOMMENDATIONS

It is recommended that the Programs Committee approve the following resolution:

RESOLVED, that the Programs Committee approve the establishment of a Leadership Bank program.

ATTACHMENT(S) LIST

- A.** Approval of Interest on Lawyers' Trust Accounts (IOLTA) Grant Distribution for 2020 Agenda Item



The State Bar *of California*

OPEN SESSION

AGENDA ITEM

131 JULY 2019

PROGRAMS COMMITTEE III.B

DATE: July 11, 2019

TO: Members, Programs Committee
Members, Board of Trustees

FROM: Corey Friedman, Co chair, Legal Services Trust Fund Commission
Christian Schreiber, Co chair, Legal Services Trust Fund Commission
Hellen Hong, Director, Office of Access & Inclusion

SUBJECT: Approval of Interest on Lawyers' Trust Accounts (IOLTA) Grant Distribution for 2020

EXECUTIVE SUMMARY

Annually, the Board of Trustees sets the grant amount available for distribution from Interest on Lawyers' Trust Accounts (IOLTA) to qualified nonprofit legal aid organizations in California. Although we refer to these funds "IOLTA grants," over the years these funds have been supplemented with Justice Gap Funds and contributions from the State Bar licensing fees. This request is for the Board to approve the distribution of grant funds for the 2020 calendar year. After careful review of the revenue projections and consideration of the needs of low-income Californians and legal aid programs, the Legal Services Trust Fund Commission recommends a calendar year 2020 grant distribution of \$55.6 million, a 102 percent increase over the 2019 grant distribution, leaving a reserve of \$29.5 million.

BACKGROUND

IOLTA STATUTE

In 1981 the Legislature authorized the Interest on Lawyers' Trust Accounts (IOLTA) program under Business and Professions Code Sections 6210-6228 (IOLTA statute) to increase access to justice and improve the administration of justice through expansion of legal services, improving

the quality of existing free legal services in civil matters to indigent persons and initiating new programs to provide such services.

The IOLTA statute requires lawyers to place client funds that are on deposit for short periods of time or of nominal amounts into interest- or dividend-bearing accounts in which the interest or dividend is paid to the State Bar. Such IOLTA accounts can only be kept at approved financial institutions certified by the State Bar to ensure compliance with the IOLTA statute. If there is a large sum of money involved, or it will be held for a long time, an attorney can hold the client's funds in an individual account, designated as a Client Trust Account, and the interest earned will go to the client.

The interest earned from pooled IOLTA accounts is remitted to the State Bar. The State Bar subtracts its administrative costs and then distributes the approved fund amount (based on the IOLTA statutory formula) to qualified legal aid nonprofit organizations who provide free legal services in civil matters to indigent persons in California. The Office of Access & Inclusion administers the Legal Services Trust Fund Program for the State Bar under the oversight of the Legal Services Trust Fund Commission (LSTFC) and Board of Trustees.

In 2007, AB 1723 (Jones, Ch. 422, Stats. of 2007) amended the IOLTA statute to specify that IOLTA accounts should earn no less than the interest rate or dividend generally available to non-IOLTA depositors at the same institution. This is referred to as “comparability.” However, since that change in the law became effective in 2008, interest rates plummeted and the IOLTA program, until recently, did not reap the anticipated benefits of comparability.

DISTRIBUTION OF IOLTA FUNDS

Each year, the Board of Trustees set the amount of IOLTA grants available for distribution to qualified nonprofit legal aid organizations who provide free legal services to indigent Californians in civil legal matters.

In the first eight grant years (1984-1992) the Legal Services Trust Fund Program set the amount for distribution for the Board’s approval as the total money projected to be “on hand” as of the end of the prior year, 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, such that 100 percent of the money for grants was “on hand” for distribution throughout the year. Financial institutions continued to remit interest earned, so the program always had on hand about one full year’s revenue.

In 1992, in response to low interest rates and declining revenue, the then Board of Governors adopted a cash-on-hand policy to hold only 75 percent of a year’s cash on hand. Over the years, subsequent interest rate declines led to further reductions to the target range to 25-30 percent.

IOLTA revenue remained flat between 2001 and 2004—hovering around \$10M—but showed a steady increase beginning with the 2005 grant year. For many legal aid organizations, IOLTA funding is core support, meaning that organizations have the flexibility to use the funds where they need it most; many other funders impose specific restrictions on funds (i.e., only salaries

but no benefits or no overhead costs). As such, these grants offer stability to grantees because the consistency and predictability in funding levels had not demonstrated significant fluctuations from year to year.

Consistent with this principle, after receiving feedback from the legal aid community, the LSTFC proposed, and the Board of Governors approved in 2006 a revision to the reserve policy (also referred to as the cash-on-hand policy. See Attachment A) to build reserve funds that could be distributed during lean years. Then, as now, the LSTFC recognized the ability to rely on stable IOLTA funding is critical to the health and survival of legal aid organizations that receive IOLTA funding.

This prudent planning to build a reserve paid off during the most recent recession. IOLTA revenue reached a high of \$20.2 million in 2008. Then, due to the recession and unprecedented low interest rates, IOLTA revenue dropped to \$7 million and stayed below that amount for nearly a decade, rising only as high as \$6.35 million in 2017. Funds put aside because of the reserve policy (and additional revenue from sources such as the Justice Gap Fund and the Legal Services Assistance Fund) supplemented low IOLTA revenue.

DISCUSSION

For the past two years the Office of Access & Inclusion has focused on re-certifying approximately 175 financial institutions offering IOLTA accounts to ensure their compliance with the IOLTA statute, particularly ensuring that IOLTA accounts are receiving comparable interest rates to similarly situated accounts. As a result, in 2019, the State Bar distributed \$27.6 million in IOLTA grants, nearly double the amount distributed in the prior year. The recent increase in IOLTA revenue is largely the result of rising interest rates and the State Bar's efforts to ensure compliance with the statutory requirements.

The chart below illustrates the changes in IOLTA grant distributions over the past five years.

Year	IOLTA Grant Distribution (in millions)	Percent Change over Previous Year
2020	\$55.6 (proposed)	102%
2019	\$27.6	97%
2018	\$14	26%
2017	\$9.1	(18%)
2016	\$11.1	10%
2015	\$10	5%

The current Federal Funds Rate is a range of 2.25 and 2.50 percent. However, it has been widely reported that the Federal Reserve may decrease the current Federal Funds Rate in 2019. A decrease in the Federal Funds Rate would likely decrease the IOLTA revenue available for the 2021 calendar year.

Taking the Federal Funds Rate and the effect on overall interest rates into consideration, staff recommended a moderate distribution level. The justification for a moderate distribution is the

projected decrease in interest rates will be balanced by the State Bar's efforts to further encourage banks to increase the rates on IOLTA accounts. We believe these factors will make the projection of the amount available for distribution and cash on hand a reasonable one.

In applying the cash-on-hand policy in 2018 and 2019, a portion of increased receipts was held in reserve as a hedge against future declines in revenue. Under the policy, when revenue is higher than in the previous year, grants are increased incrementally while also increasing the reserve/cash on hand. The cash-on-hand policy applies the following methodology:

- First, the previous year's grant distribution is established as the planned grant distribution base amount
- Second, the planned grant distribution base is increased by 5 percent over the prior year's amount
- Then 10 percent of the prior year's grant distribution is set aside to the reserve/cash on hand
- Any remainder in the projected net assets is split equally, increasing both grant distribution and reserve/cash on hand

Attachment B lays out the calculation, showing the anticipated revenues, the proposed distribution based on application of the cash-on-hand policy, and the amount of reserves that would be remaining for future years. In short, the LSTFC and staff recommend a 2020 distribution of \$55.6 million, while leaving \$29.5 million in reserve.

If revenue is insufficient to cover projected grant distributions, the State Bar has no obligation to fund the grants beyond the revenue received. However, the LSTFC recognizes that it would be an immense hardship to grantees, and ultimately low-income Californians, if the Legal Services Trust Fund program was unable to satisfy fully the grant amounts identified at the start of the year, and therefore consistently projects revenues conservatively.

IOLTA LEADERSHIP BANK PLAN

Historical Context

As mentioned above, in 2007, AB 1723 (Jones) amended the IOLTA statute to specify that IOLTA accounts should earn no less than the interest rate or dividend generally available to non-IOLTA depositors at the same institution. Prior to that, financial institutions had no obligation to offer comparable interest rates on IOLTA accounts.

In 2008, the State Bar adopted revisions to the State Bar Rules to reflect the comparability law, mandating that IOLTA-eligible institutions pay comparable interest rates or dividends on their IOLTA accounts in one of three ways:

1. Establish IOLTA accounts as comparable-rate products;
2. Pay the comparable-product rate on IOLTA deposits accounts, less chargeable fees, if any; or
3. Pay the Established Compliance Rate (known as ECR) determined by the Legal Services Trust Fund Commission. (See Rule 2.130.)

The Legal Services Trust Fund Commission set the Established Compliance Rate at 68 percent of the Federal Funds Rate (FFR) in 2008.

However, in 2008, the nation was in the midst of the great recession and the Federal Funds Rate was 0.25 percent - the lowest possible rate. This FFR was not increased until December 2015 to 0.50 percent. For the past two years, the FFR has steadily been increasing. The chart below summarizes the relation of the FFR and the amount of IOLTA revenue the State Bar projected for distribution for the following year to support free civil legal services.

Year	Federal Funds Rate at Year End	Approximate IOLTA Interest Revenue Distributed the following year* (in millions)
2015	0.50%	\$5.2
2016	0.75%	\$6.0
2017	1.50%	\$6.5
2018	2.25%	\$20.1
2019	2.50%	\$39.0

(*Note that this differs from the total grant distributions those years, which includes contributions from licensee fees, the Justice Gap Fund and other sources).

Current IOLTA Interest Rate Landscape

In California, financial institutions currently hold about \$5 billion in IOLTA deposits. For the past 18 months, the State Bar has focused on certifying nearly 200 financial institutions that hold IOLTA accounts to ensure that financial institutions are offering similar interest and dividend rates on their IOLTA products to similarly situated depositors. If we do not certify them, they will no longer be eligible to offer IOLTA accounts to California licensees. This certification process requires individual review of each financial institution's various account products, a determination of which products are available for accounts similar to IOLTA depositors, and, if financial institutions do not elect the ECR, confirming that the rate offered for IOLTA accounts is comparable to that offered on accounts for similarly-situated depositors.

The top 20 financial institutions with the largest deposits of IOLTA accounts hold 86 percent of the \$5 billion of deposits in California IOLTA accounts. For those top 20 financial institutions, the interest rates paid on IOLTA accounts range from 0.05 percent to 1.73 percent. In 2019, if all of the top 10 financial institutions elected to pay the ECR – currently 1.70 – that decision would yield **an increase of \$23 million** in additional funds to support free civil legal services to low-income Californians (assuming FFR remain static). The chart below highlights, for the 10 financial institutions holding the largest deposits amounts in IOLTA accounts, whether the institution has elected the ECR, and if not, the estimated average interest paid on IOLTA accounts in California, which often fluctuates based on tiered rates on sizes of deposit accounts.

Financial Institution	Average IOLTA Balances from April/May 2019 (in millions)	Percentage of IOLTA Deposits in California	ECR or Average Interest Paid on IOLTA accounts	Potential Additional Revenue for Civil Legal Services if at ECR
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City National Bank	\$ 430.2	8.90%	0.28%	\$ 6.2 million
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Total	\$3.572B	74%		\$16.8 million

Of the 160 financial institutions eligible to hold IOLTA accounts (there have been mergers since the start of the certification process), staff have only 27 remaining to review to confirm that they are providing comparable rates to their IOLTA accounts. Along with this certification process, the State Bar will be focusing on compliance; ensuring that these financial institutions continue to remit the correct interest rates on the nearly 50,000 IOLTA accounts.

Leadership Bank Proposed Program

In order to advance the State Bar's goal to increase access to justice, the State Bar is advancing a "Leadership Bank" program to encourage financial institutions to do the following:

1. Elect at least the ECR rate of 68 percent of the Federal Funds Rate on all accounts;
2. Waive any fees or charges on these accounts; and
3. Utilize the Bank State Bar IOLTA portal and remit payments to the State Bar.

The Leadership Bank Program would increase revenue to support civil legal services and streamline operations for the State Bar of California. These "Leadership Banks" would be highlighted on the State Bar's website as preferred IOLTA eligible institutions because they

provide increased revenue for free civil legal services. The State Bar would highlight these institutions as lead partners supporting access to justice through the IOLTA program.

The Office of General Counsel has conducted an analysis of the permissibility of such a Leadership Program and has concluded that it is permissible for the State Bar to highlight businesses that meet criteria that further government objectives. Recognizing financial institutions that pay higher interest rates, like the ECR and above, increases revenue for the State Bar Legal Services Trust Fund program, which directly advances the State Bar's statutory mission of "support[ing] greater access to...the legal system." California Business and Professions Code Section 6001.1.

To offer all institutions an opportunity to become a Leadership Bank, the State Bar plans to release information to all institutions later in the summer of 2019 and issue a news release with the list and benefits of "Leadership Banks" in the fall of 2019.

FISCAL/PERSONNEL IMPACT

The recommended distribution is net of the \$2.1 million projected costs to administer the program. Administration of the IOLTA program is fully funded through IOLTA revenue. This recommendation does not affect the general fund budget. No additional staff or other expenses will be incurred as a result of the adoption of recommendation.

RULE AMENDMENTS

None

BOARD BOOK AMENDMENTS

None

STRATEGIC PLAN GOALS & OBJECTIVES

Goal: 4. Support access to legal services for low- and moderate-income Californians and promote policies and programs to eliminate bias and promote an inclusive environment in the legal system and for the public it serves, and strive to achieve a statewide attorney population that reflects the rich demographics of the state's population.

Objective: a. Support increased funding and enhanced outcome measures for Legal Services

RECOMMENDATIONS

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

RESOLVED, that the Board of Trustees approve the recommendation of the Legal Services Trust Fund Commission to approve the distribution of \$55,581,082 in IOLTA grants for the 2020 calendar year, while setting aside a reserve of \$29,491,209.

ATTACHMENT(S) LIST

- A. State Bar 2006 Cash On Hand Policy/Reserve Policy
- B. Proposed IOLTA 2020 Grant Distribution Funding Detail

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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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 \$1,200,560 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.

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

Proposed IOLTA 2020 Grant Distribution Funding Detail

Projected Available Funds for 2020 Grants

A. Revenue - January through December 2019	
Jan-March actual IOLTA Revenue	\$ 10,851,720
April-Dec projected IOLTA Revenue	30,384,816
Justice Gap Funds including cy pres	1,000,000
Fee Statement Contributions	6,000,000
Projected Interest & Tax Intercept Funds	250,000
Total Revenue:	48,486,536
B. Expenses - January through December 2019	
IOLTA Grant Distributions - 2019	27,463,024
Administration, Net of EAF & Bank Settlement	2,100,000
Total Expenses:	29,563,024
C. Projected 2019 Revenue less Grants & Admin Expenses	\$ 18,923,512
D. Projected Net Assets at December 2019	
Available Net Assets at 12/31/2018	24,082,586
Projected Revenue over Expenses 2019	18,923,512
Projected 2019 Ending Net Assets:	\$ 43,006,098
E. 2020 Projected Revenue & Expenses	
IOLTA Revenue	39,066,192
Justice Gap Revenue	900,000
Fee Statement Contributions - assume decrease	4,000,000
Interest Income & Tax Intercept Funds	250,000
Administration, Net of EAF & Bank Settlement	(2,250,000)
2020 Revenue after Administrative Expenses:	41,966,192
Projected 2019 Ending Net Assets:	43,006,098
Funds Available:	\$ 84,972,290
F. Grants	
Grant distribution 2019 (baseline)	27,463,024
5% of 2019 Grants to Programs	1,373,151
Remainder Split between Reserve/Cash and Grants	26,694,907
Total 2020 Grants:	\$ 55,531,082
Percentage Increase over 2019 Grant Allocation:	102%
G. Reserve/Cash on Hand/Net Assets	
10% of 2019 Grants to Stabilization Reserve	2,746,302
Remainder Split between Reserve/Cash and Programs	26,694,907
Projected Reserve/2020 Ending Net Assets:	\$ 29,441,209
Reserve as Percentage of 2020 Grants*:	53%

* Materials from the March 2006 Board of Governors meeting indicate that reserves should be maintained between 30% and 75% of current grant amounts.