

# The State Bar of California

## Client Security Fund - 2008 Activities Report

### Public Protection Program

The Client Security Fund, established by bar-sponsored legislation in 1972, represents one of the State Bar's major efforts to achieve its public protection goals. In addition to disciplinary procedures, as part of the Bar's public service, the Fund helps to alleviate injury to legal consumers who sustain money or property loss as the result of dishonest conduct by a member of the Bar. The Fund is designed to reimburse victims who have lost money or property due to theft, or an act equivalent to theft, committed by a lawyer acting in a professional capacity.

The Fund provides the legal profession with a unique opportunity to promote public confidence in the administration of justice and the integrity of the legal profession. It is also a cost-effective way of providing reimbursement to victims that is generally not available from any other source. The Client Security Fund works closely and cooperatively with the State Bar's lawyer discipline system and the State Bar Court to achieve the Fund's objectives--to come to the aid of those clients who have suffered a loss caused by a diminutive number of errant lawyers.

In 2008, the Fund was financed primarily by a \$40 annual assessment added to the membership dues paid by California active lawyers and a \$10 annual assessment paid by inactive lawyers. The Fund reimburses eligible applicants up to a \$50,000 maximum payment. However, there is no limitation on the aggregate amount paid against a Respondent lawyer. Since its inception, the Fund has reimbursed applicants approximately \$89.6 million. In 2008, the Fund paid \$4,638,272 on 479 awards. The most typical losses reported are theft of client personal injury settlement funds and the failure to refund fees when the lawyer performs no work.

### Rules and Coverage

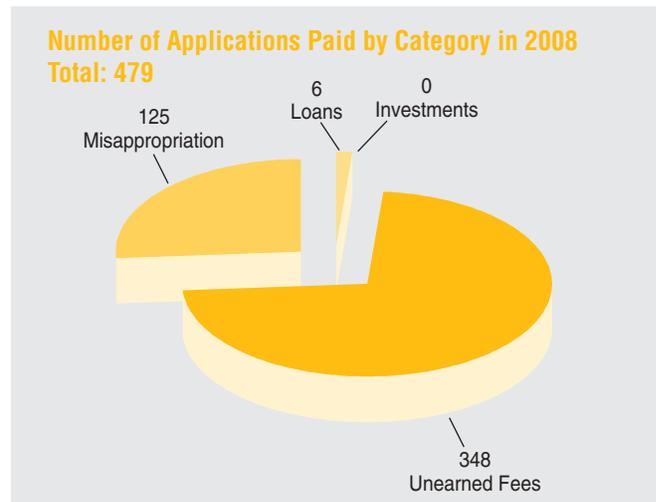
The Fund is governed by the Rules of Procedure, Client Security Fund Matters which were adopted by the Board of Governors on December 21, 1985. Under these Rules, a seven-member Commission, appointed by the Board, acts as the Board's delegate in administering the Fund. From time to time, the Commission recommends to the Board amendments to the Rules of Procedure. Proposed rule changes are circulated for public comment before final action is taken by the Board.

The rules set forth the scope and purpose of the Fund, the authority of the Commission, the requirements for reimbursement, the application process, the confidentiality of the Fund records, and judicial review of Commission decisions. An applicant or Respondent lawyer may seek judicial review of a Final Decision of the Commission in the superior courts of the State under section 1094.5 of the Code of Civil Procedure.

### Number of Applications Paid by Category

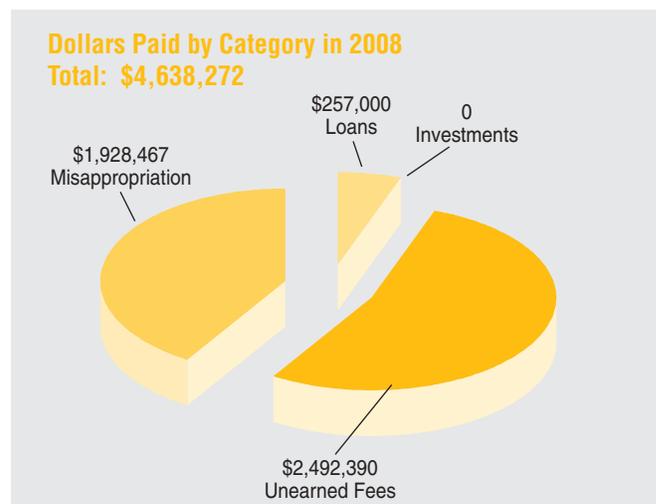
In 2008, the Fund paid out \$4,638,272 on 479 awards.

The largest number of applications paid was in the "unearned fees" category (72.7%). The second largest category by size was "misappropriation" (26%) with "loans" and "investments" representing less than 2% of the applications paid.



### Dollar Amount of Applications Paid by Category

In 2008, "Unearned Fees" cases represented the largest dollar amount of applications paid, \$2,492,390 or approximately 53.7 percent. The second largest dollar amount of applications paid was in the "Misappropriation" category, \$1,928,467, represented approximately 41.6 percent. The remaining few percent of the total payouts was "Loans."



## General Basis for Reimbursement

An applicant must establish the loss of money or property which came into the hands of an active member of the State Bar while acting as a lawyer, trustee or fiduciary as defined in the Rules of Procedure, Client Security Fund Matters, and which loss was caused by a dishonest act as defined under the rules.

## Rule of Limitations

Applications for reimbursement from the Fund must be filed within four years after the applicant discovers or reasonably should have discovered the loss.

## Status of the Lawyer

In order for reimbursement to be paid, the lawyer whose dishonest conduct caused the loss must have been acting as a lawyer, or in a specified fiduciary capacity, such as the trustee of an express trust or as an escrow holder.

Also, the lawyer must have been disciplined, voluntarily resigned, died, been found mentally incompetent or been judged guilty of a crime that involved the loss. The Rules do give the Commission the discretion to waive this requirement under certain limited circumstances - for example, in clear cases when formal charges have been filed but the lawyer has not yet been disciplined.

## Dishonest Conduct

A lawyer's dishonest conduct that can lead to payment from the Fund includes:

- theft or embezzlement of money or the wrongful taking or conversion of money or property;
- refusal to refund unearned fees received in advance where the lawyer performed no services or an insignificant part of the services contracted for such that the lawyer can be regarded as having lacked the intention to perform at the time payment was received;
- the borrowing of money from a client without the intention or the reasonably anticipated ability to repay it;
- obtaining money or property from a client by representing that it would be used for investment purposes when no investment is made; or
- an act of intentional dishonesty or deceit which directly leads to the loss of the money or property.

## Losses not Covered

The Fund will not reimburse a loss if:

- it was covered by insurance, a bond or another fund;
- it was caused by negligence or malpractice; or
- it was a bad business loss such as a failed investment.

The Fund also does not cover "interest," "incidental or consequential losses" or "expenses" caused by the attorney. Examples of incidental or consequential losses would include fees applicant paid to another attorney or damages caused by malpractice, negligence or incompetence.

*"Thanks for taking time and prompt attention to our case. We're really grateful to the State Bar of California for helping us and reimbursing us."*

(Quote from Applicant 2008)

## Legislation

Oversight of the Client Security Fund is provided by the Legislature through a series of statutes, and by the Bar's Board of Governors through the Rules of Procedure, Client Security Fund Matters.

The State Bar's authority to operate the Client Security Fund is found in Business & Professions Code section 6140.5. This Legislation, effective March 4, 1972, was a result of a Board resolution dated June 17, 1971 and a Bar-sponsored bill. Section 6140.5(a) requires the Board to maintain a Client Security Fund.

Effective January 1, 2006, Section 6140.5(a) was amended to expand the purpose of the Client Security Fund to include relieving or mitigating pecuniary losses caused by the dishonest conduct of Foreign Legal Consultants registered with the State Bar and attorneys registered with the State Bar under the Multi-jurisdictional Practice Program.

Section 6140.5(b) provides a special statute of limitations whereby the Bar may bring an action to enforce its subrogation rights within three years of the date of payment to an applicant. Another part of the Bar's effort to collect against the errant lawyer is section 6140.5(c) which allows the Bar to add any CSF payout, plus interest and processing costs, to the membership dues bill of any lawyer who has been disciplined or resigns with discipline matters pending and seeks to be reinstated.

Section 6140.5(d) allows certain fund payments to be enforced as money judgments pursuant to Division 2 (commencing with Section 695.010) of the Code of Civil Procedure. This subdivision does not limit the power of the Supreme Court to alter the amount owed or to authorize the State Bar Court, in the enforcement of a judgment under this subdivision, to approve an agreement for the compromise of that judgment.

Section 6140.55 currently allows the Board to assess annually up to \$40 per active member and \$10 per inactive member to support the Fund. This assessment is to be used only for the purposes of the Fund.

Section 6149.5 serves as an early loss prevention measure. It requires insurers to provide written notice to a claimant of settlement payments of \$100 or more delivered to the claimant's lawyer or other representative in settlement of any third-party liability claim.

Another statute that affects the Fund is section 473 of the Code of Civil Procedure. Under this section, when a court sets aside a default judgment due to a party or attorney's mistake, inadvertence, surprise or excusable neglect, it may (1) impose a penalty of no more than \$1,000, (2) direct the offending attorney to pay up to \$1,000 to the Client Security Fund, or (3) grant such other relief as appropriate. Under this statute, the Fund received \$16,425 in 2008.

*"Your efficiency means a lot to me and my family and gives many hopes to those victims like us."*

(Quote from Applicant 2008)

## CLAIMS ACTIVITY 2000 - 2008

### Nine-year Comparison

	# of Claims	2000 Amount	# of Claims	2001 Amount	# of Claims	2002 Amount	# of Claims	2003 Amount	# of Claims	2004 Amount	# of Claims	2005 Amount	# of Claims	2006 Amount	# of Claims	2007 Amount	# of Claims	2008 Amount
Claims outstanding, beg. of year	758	10,345,650	708	8,803,264	751	9,517,404	770	10,157,007	759	8,548,576	858	9,956,622	787	10,396,199	797	9,579,525	787	11,811,143
Prior year's outstdg. claim adj. inc.	(4)	(10,043)	(2)	110,553	5	29,491	(2)	55,611	(13)	109,900	(3)	90,040	(2)	241,984	-	69,048	-	107,497
New claims	1,049	10,929,128	1,114	11,900,739	1,300	14,166,217	1,200	12,221,905	1,321	13,681,482	1,318	11,558,645	1,314	10,916,591	1,013	12,927,446	825	11,290,084
<b>TOTAL CLAIMS</b>	<b>1,803</b>	<b>21,264,735</b>	<b>1,820</b>	<b>20,814,556</b>	<b>2,056</b>	<b>23,713,112</b>	<b>1,968</b>	<b>22,434,523</b>	<b>2,067</b>	<b>22,339,958</b>	<b>2,173</b>	<b>21,605,307</b>	<b>2,099</b>	<b>21,554,774</b>	<b>1,810</b>	<b>22,576,019</b>	<b>1,612</b>	<b>23,208,724</b>
Less: Processed Claims:																		
Paid	595	3,673,850	609	4,435,212	782	6,597,057	701	5,859,620	746	5,681,455	982	4,648,584	943	5,299,061	607	4,352,110	479	4,638,272
Rejected	132	4,061,716	68	2,903,338	39	2,580,784	39	2,585,959	39	1,701,671	50	2,535,698	24	1,799,629	42	2,066,308	57	2,196,878
Withdrawn	368	4,725,923	392	3,958,602	465	4,378,264	469	5,440,368	424	5,000,210	354	4,024,826	335	4,876,599	374	4,346,458	366	4,502,033
<b>TOTAL PROCESSED CLAIMS</b>	<b>1,095</b>	<b>12,461,489</b>	<b>1,069</b>	<b>11,297,152</b>	<b>1,286</b>	<b>13,556,105</b>	<b>1,209</b>	<b>13,885,947</b>	<b>1,209</b>	<b>12,383,336</b>	<b>1,386</b>	<b>11,209,108</b>	<b>1,302</b>	<b>11,975,249</b>	<b>1,023</b>	<b>10,764,876</b>	<b>902</b>	<b>11,337,183</b>
Claims outstanding, end of year	708	8,803,264	751	9,517,404	770	10,157,007	759	8,548,576	858	9,956,622	787	10,396,199	797	9,579,525	787	11,811,143	710	11,871,541
Claims outstanding inc./(dec.) over beginning balance	(50)	(1,542,386)	43	714,140	19	639,603	(11)	(1,608,431)	99	1,408,046	(71)	439,577	10	(816,674)	(10)	2,231,618	(77)	60,398
Claims payout ratio		30.20%		33.75%		44.20%		45.26%		43.88%		43.79%		42.86%		42.45%		40.68%
Est. claims Fab at payout ratio		2,658,586		3,212,124		4,489,397		\$3,869,086		4,368,966		4,552,496		4,105,784		5,013,830		4,829,343
<b>NET ASSETS</b> (end of year)		8,981,524		9,022,435		5,656,285		\$4,303,609		2,229,455		1,479,897		2,325,593		2,990,889		4,304,519
<b>NET ASSETS</b> (end of year, cash-basis)		11,640,110		12,234,559		10,145,682		8,172,695		6,598,421		6,032,393		6,431,377		8,004,719		9,133,862

# Financial Picture

To have a complete picture of the Fund's fiscal health, it is important not only to see what money is on hand and how much has been actually paid out, but to also know how much is expected to be paid on pending cases. This anticipated payout, or accrued liability, is calculated by multiplying the total dollar amount of the pending cases times an estimated claims payable ratio. The claims payable ratio is based upon how much the Fund has historically paid for every dollar claimed. For example, if the Fund has historically paid \$.30 for every \$1 claimed, then the claims payable ratio is 30 percent.

The claims payable ratio used by the Fund is based upon a 24-month rolling average. The accrued liability changes, not only with changes in the claims payable ratio, but also as the total dollar amount of outstanding applications changes.

## Balance Sheet

The balance sheet shows the Fund's assets and liabilities as of December 31, 2008.

Fund assets are maintained in cash and cash equivalents.

Current liabilities include estimated awards ultimately to be paid on applications which are pending as of December 31 plus next year's dues payments received early - for example, 2008 dues received in 2007.

The Fund balance or deficit is simply the difference between Fund assets and accrued liabilities.

## Statement Of Revenues, Expenses And Changes In Fund Balance

Total revenues consist of members' dues, interest income and other revenues such as contributions.

Expenses include awards paid, accrued liabilities and administrative expenses. Awards constitute the major element. Off-set against this expense are any monies recovered from the bar's collection activities. This is reflected as "Awards Reimbursements or Recovery."

The Estimated Decrease/(Increase) in Awards Payable Liability is an adjustment made at the end of the year because of a change in the accrued liability.

*"I want to extend my gratitude for your expeditious and professional handling of this claim."*

(Quote from Applicant 2008)

*"We're are really grateful to the State Bar of California for helping us and reimbursing money to us."*

(Quote from Applicant 2008)

### 2006 - 2008 BALANCE SHEET STATEMENTS

	AUDITED 12/31/06	AUDITED 12/31/07	UNAUDITED 12/31/08
<b>ASSETS:</b>			
Cash	7,708,941	9,464,048	10,579,890
<b>LIABILITIES &amp; FUND BALANCES:</b>			
Current liabilities	5,383,348	6,473,159	6,275,371
Net Assets	2,325,593	2,990,889	4,304,519
Total liabilities & Fund balances	7,708,941	9,464,048	10,579,890

### 2006 - 2008 STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES

	AUDITED 12/31/06	AUDITED 12/31/07	UNAUDITED 12/31/08
<b>REVENUES:</b>			
Membership dues	6,349,590	6,536,140	6,715,339
Investment Income	427,548	529,984	422,005
Other/Miscellaneous Revenues	5,103	-	-
<b>TOTAL REVENUES</b>	<b>6,782,241</b>	<b>7,066,124</b>	<b>7,137,344</b>
<b>EXPENSES:</b>			
Awards Paid/Accrued	4,836,217	5,289,156	4,458,375
Less: Awards Reimbursements or Recovery	(575,041)	(539,728)	(425,949)
CSF Claims Collection Exp.	9,287	19,375	56,920
Total	4,270,463	4,768,803	4,089,346
Administration	1,666,082	1,632,026	1,734,368
<b>TOTAL EXPENSES</b>	<b>5,936,545</b>	<b>6,400,829</b>	<b>5,823,714</b>
<b>EXCESS (DEFICIT) OF REVENUES OVER EXPENSES</b>			
	845,696	665,295	1,313,630
<b>Estimated Decrease / (Increase) in Awards Payable Liability</b>			
	446,712	(908,046)	184,487
<b>Net Assets, as of year-end</b>	<b>2,325,593</b>	<b>2,990,889</b>	<b>4,304,519</b>

*"I cannot express my overall joy as now I can pay the new attorney for his legal representation of my niece."*

(Quote from Applicant 2008)

## Commission Members



**Donna C. Riegel**, an attorney member, is currently a sole practitioner in Pasadena with extensive and varied civil litigation experience. She has been a volunteer temporary judge with the Los Angeles County Superior Courts. She was appointed in October 2004 and serves as Chair for 2008-2009. Her term expires in September 2009.



**Joyce L. Hurley**, a public member, is a paralegal in a private legal firm in Los Angeles. She was appointed in September 2005 and serves as Vice-Chair for 2008-2009. Her term expires in September 2009.



**Howard Caldwell**, a public member, is a self-employed consultant in labor management relations. He was appointed in September 2008. His term expires in August 2011.



**Richard C. Henderson**, an attorney member, is currently a sole practitioner in Fresno. He was appointed in September 2007. His term expires in September 2010.



**Paul S. Hokokian**, an attorney member and former Board member, is currently a sole practitioner in Fresno. He was appointed in September 2008. His term expires in August 2011.



**Wendy Oshiro**, an attorney member, is currently a real estate analyst in Los Angeles. She was appointed in September 2008. Her term expires in August 2011.



**Earl Paysinger**, a public member, is currently Assistant Chief in the Los Angeles Police Department. He has served in a variety of command assignments and is currently the Director of Operations for the LAPD. He was appointed in October 2006. His term expires in September 2009.

*"This is a letter of great gratitude and appreciation."*

(Quote from Applicant 2008)

*"I once again trust our legal system."*

(Quote from Applicant 2008)

## Decision Making

Policy oversight of the Client Security Fund is a joint responsibility of the Board of Governors and the Client Security Fund Commission.

The Board monitors the Fund through its: appointment of seven commissioners; approval of recommended changes and additions to the Rules of Procedure; consideration and approval of the Fund's annual administrative budget; and power to seek legislative authority to increase the lawyer's fees that support the Fund.

The Board exercises its authority as an entity and through its Regulation, Admissions, and Discipline Oversight Committee (RAD).

Of the seven volunteer members who comprise the Commission, no more than four of them may be lawyers. They are assisted by a professional staff of 9 who screen, analyze, investigate and present cases to the Commission. Staff is subject to Management oversight and reports to Scott J. Drexel, the Chief Trial Counsel for the State Bar's discipline system.

Among the Commission's key functions are:

- determining applications made to the Fund after a written and oral presentation of the matter by CSF staff and, occasionally, after hearing held before the Commission;
- recommending to the Board of Governors necessary staffing levels to carry out the Fund's business in a professional, timely fashion;
- taking steps to increase the efficiency and timeliness with which the Commission and staff process applications;
- monitoring the Fund balance and recommending to the Board of Governors necessary fee increases to guarantee its continued solvency;
- interpreting the Rules of Procedure through policy statements and recommending necessary amendments and additions; and
- providing for the efficient inner workings of the Commission itself.



### THE STATE BAR OF CALIFORNIA

Client Security Fund  
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