

The State Bar of California

Client Security Fund - 2009 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.

The Fund is primarily financed by an annual assessment added to the membership dues paid by California lawyers (currently \$40 per active member and \$10 per inactive member). These assessments are applied only for the purposes of Fund payments and costs associated with the Fund's administration. Effective January 1, 2009, the Board of Governors increased the maximum payment to an applicant from \$50,000 to \$100,000 for losses occurring on or after January 1, 2009. The Board also eliminated the "marriage penalty" by allowing spouses to be treated as separate applicants.

Beginning in August of 2009, the filing rate for new applications began to increase significantly due to loan modification losses. On December 31, 2009, the Fund had 3,028 applications pending as compared to the 902 pending at year end 2008. The Client Security Fund estimates that at least 2,000 of the 3,028 cases, pending are based on loan modification losses. Since its inception, the Fund has reimbursed applicants approximately \$93 million. In 2009, the Fund paid \$3,461,950.00 on 378 awards. The most typical losses reported are theft of client personal injury settlement funds, and failure to refund fees when the lawyer performed no work, which includes losses caused by the loan modification schemes.

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. In 2009, the Board adopted new rules for the Client Security Fund which will apply to all cases filed on or after January 1, 2010. The new rules simplified the language but did not result in substantive changes.

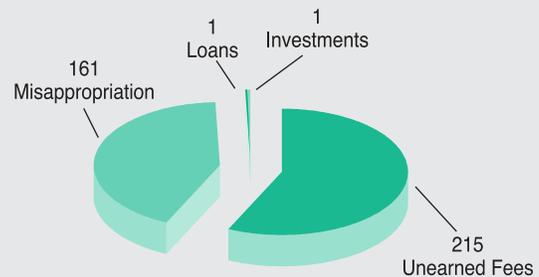
The rules set forth the scope and purpose of the Fund, the authority of the Commission, the requirements for reimbursement, the application process, the confidentiality of the Fund records, and judicial review of Commission decisions. An applicant or Respondent lawyer may seek judicial review of a Final 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 2009, the Fund paid out \$3,461,950 on 378 awards.

The largest number of applications paid was in the "unearned fees" category (56.9%). The second largest category by size was "misappropriation" (42.6%) with "loans" and "investments" representing less than 1% of the applications paid.

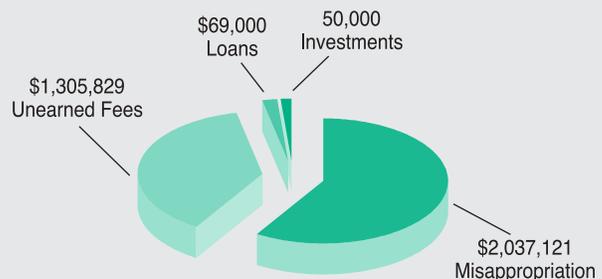
Number of Applications Paid by Category in 2009
Total: 378



Dollar Amount of Applications Paid by Category

In 2009, while "Unearned Fees" cases comprised the largest number of applications filed, "misappropriation" cases comprised the largest dollar amount of applications paid, \$2,037,121 or approximately 58.8 percent. "Unearned Fees" cases comprised the second largest dollar amount of applications paid, \$1,305,829 or approximately 37.7 percent. The remaining few percent of the total payouts were "Loans" and "Investments."

Dollars Paid by Category in 2009
Total: \$3,461,950



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.

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 \$9,630 in 2009.

"Just a few lines to say thank you for standing by me even when I was about to give up. And thanks for your courtesy. You always returned my calls and you never got impatient on the phone."

(Quote from Applicant 2009)

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, 2009.

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, 2009 dues received in 2008.

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 Court ordered sanctions and occasional 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.

"Thank you very much for your decision to return our retainer. This has been a major hardship on us and we appreciate your integrity."

(Quote from Applicant 2009)

"Please accept my sincerest appreciation for granting my request for the reimbursement from the Client Security Fund."

(Quote from Applicant 2009)

2007 - 2009 BALANCE SHEET STATEMENTS

	AUDITED 12/31/07	AUDITED 12/31/08	UNAUDITED 12/31/09
ASSETS:			
Cash	9,464,048	10,579,890	11,474,118
LIABILITIES & FUND BALANCES:			
Current liabilities	6,473,159	6,275,371	8,795,297
Net Assets	2,990,889	4,304,519	2,678,821
Total liabilities & Fund balances	9,464,048	10,579,890	11,474,118

2007 - 2009 STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES

	AUDITED 12/31/07	AUDITED 12/31/08	UNAUDITED 12/31/09
REVENUES:			
Membership dues	6,536,140	6,715,339	6,872,572
Investment Income	529,984	422,005	145,501
Other/Miscellaneous Revenues	-	-	6,500
TOTAL REVENUES	7,066,124	7,137,344	7,024,573
EXPENSES:			
Awards Paid/Accrued	5,289,156	4,458,375	7,343,982
Less: Awards Reimbursements or Recovery	(539,728)	(425,949)	(615,485)
CSF Claims Collection Exp.	19,375	56,920	62,933
Total	4,768,803	4,089,346	6,791,431
Administration	1,632,026	1,734,368	1,858,840
TOTAL EXPENSES	6,400,829	5,823,714	8,650,271
EXCESS (DEFICIT) OF REVENUES OVER EXPENSES	665,295	1,313,630	(1,625,698)
Estimated Decrease / (Increase) in Awards Payable Liability	(908,046)	184,487	(3,883,423)
Net Assets, as of year-end	2,990,889	4,304,519	2,678,821

"Thank you very much for all the attention paid to and the time thus spent on the matter."

(Quote from Applicant 2009)

Commission Members



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 Chair for 2009-2010. Her 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 and serves as Vice Chair for 2009-2010. His term expires in August 2011.



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.



Colleen Dietz, a public member, is a Director of Professional Development Programs, at USC. She was appointed in September 2009. Her term expires in September 2012.



Douglas J. Hartsough, an attorney member, is currently a sole practitioner in Brentwood in Northern California. He was appointed in November 2009. His term expires in September 2010.



Linda Monroe, an attorney member, is currently a sole practitioner. She was appointed in September 2009. Her term expires in September 2012.



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.

"We want to thank you for assisting us in processing our claim."

(Quote from Applicant 2009)

"Thanks again for being so supportive and patient with us."

(Quote from Applicant 2009)

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 seven member Commission acts as the Board's delegate in administering the Fund.

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 Discipline Oversight Committee (DOC).

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 as of June 2009 reports to Colin Wong, the Chief Administrative Officer of the State Bar Court.

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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Los Angeles, CA 90015-2299
(213) 765-1140
www.calbar.ca.gov
Discipline Complaint Hotline: (800) 843-9053

CLAIMS ACTIVITY 2001 - 2009

Nine-year Comparison

	# 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	# of Claims	2009 Amount
Claims outstanding, beg. 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
Prior year's outstdg. claim adj. inc.	(2)	110,553	5	29,491	(2)	55,611	(13)	109,900	(3)	90,040	(2)	241,984	-	69,048	-	107,497	-	15,532
New claims	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	3,028	19,469,661
TOTAL CLAIMS	1,820	20,814,556	2,056	23,713,112	1,968	22,434,523	2,067	22,339,958	2,173	21,605,307	2,099	21,554,774	1,810	22,576,019	1,612	23,208,724	3,738	31,356,734
Less: Processed Claims:																		
Paid	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	378	3,461,950
Rejected	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	52	1,930,226
Withdrawn	392	3,958,602	465	4,378,264	469	5,440,368	424	5,000,210	354	4,024,826	335	4,876,559	374	4,346,458	366	4,502,033	311	3,839,708
TOTAL PROCESSED CLAIMS	1,069	11,297,152	1,286	13,556,105	1,209	13,885,947	1,209	12,383,336	1,386	11,209,108	1,302	11,975,249	1,023	10,764,876	902	11,337,183	741	9,231,884
Claims outstanding, end of year	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	2,997	22,124,850
Claims outstanding inc./(dec.) over beginning balance	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	2,287	10,253,309
Claims payout ratio		33.75%		44.20%		45.26%		43.88%		43.79%		42.86%		42.45%		40.68%		39.38%
Est. claims Fab at payout ratio		\$3,212,124		\$4,489,397		\$3,869,086		\$4,368,966		\$4,552,496		\$4,105,784		\$5,013,830		\$4,829,343		\$8,712,766
NET ASSETS (end of year)		\$9,022,435		\$5,656,285		\$4,303,609		\$2,229,455		\$1,479,897		\$2,325,593		\$2,990,889		\$4,304,519		\$2,678,821
NET ASSETS (end of year, cash-basis)		\$12,234,559		\$10,145,682		\$8,172,695		\$6,598,421		\$6,032,393		\$6,431,377		\$8,004,719		\$9,133,862		\$11,391,587