

# AGENDA ITEM

## MAR 54-165

Legal Services Trust Fund Program:  
Set Amount for Distribution for  
2009-2010 IOLTA Grants—  
Proposed Approval

DATE: February 17, 2009

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

FROM: Stephanie Choy, Managing Director, Legal Services Trust Fund Program

SUBJECT: Legal Services Trust Fund Program:  
Set Amount for Distribution for 2009-2010 IOLTA Grants—Proposed  
Approval

### EXECUTIVE SUMMARY

Each year, the Board of Governors sets the grant amount available for distribution from Interest on Lawyers' Trust Accounts ("IOLTA"). Since 1992, the distribution amount has been calculated by using a process that determines the amount of prior year's revenue, subtracts administrative costs, then adjusts the net revenue figure 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. Our calculations for 2008-09 grants included projected revenue increases due to comparability as well as donations to the Justice Gap Fund. While implementation of the comparability rule resulted in revenue increases through the spring and summer of 2008, repeated interest rate reductions in recent months will undoubtedly erase earlier gains, and result in net reductions from previous years. For 2009-2010 grants, we calculated an amount for distribution following an in-depth analysis of the Trust Fund Program's balance sheets and using projections based on reduced IOLTA revenue, Justice Gap donations and funds to be released from reserves.

Questions regarding this agenda item should be directed to Stephanie Choy, Managing Director, Legal Services Trust Fund Program (415) 538-2249.

### BACKGROUND

The Board of Governors each year sets an amount for distribution of 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 recipient programs of a grant amount, give them 30 days to prepare proposed budgets, review the budgets, fully execute grant agreements, and begin to distribute funds in July.

For each of the first eight grant periods (1984 - 1992), the amount approved for distribution was the total money projected to be on hand as of the end of the 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. At the beginning of the grant year, 100% of the money for grants was "on hand" for distribution throughout the following year. While funds were disbursed in quarterly payments, financial institutions continued to remit interest earned, so the program always had on hand about one full year's revenue.

In response to low interest rates and declining revenue, in 1992 the Board of Governors adopted the recommendations of the Trust Fund Commission and the Legal Aid Association of California, to hold less than a year's cash on hand to enable releasing more funds for immediate distribution. That year, the target cash on hand was set at 75% of the prior year's grant. In response to subsequent and dramatic interest rate declines, the target was reduced to 60% and then to 30%, where it remained for a 14-year period until 2006, when the Board of Governors (on the recommendation of the Trust Fund Commission, again after vetting the issue with the legal aid community) adopted a proposal to revise the cash on hand policy to build a reserve to stabilize grant awards in lean years.

Under this policy, when revenue is higher than the prior year, grants are held to a smaller increase so as to build a reserve to stabilize grants. In years when revenue is decreasing, the reserve can be spent down in an attempt to maintain grant levels. The following three-step calculation was applied whenever anticipated revenue exceeded prior year grants: 1) the first 5% of any increase in revenue was distributed to legal aid programs; 2) the next 10% increase in revenue was held by the LSTFP in a stabilization reserve fund; and, 3) if projected revenue exceeded 15%, then the additional amount was divided equally between increased grants and increased reserve, up to a cap of 75% of the previous year's available funds. As of June 30, 2008, in addition to 30% cash on hand of \$4,656,134, the LSTFP had built reserves of \$15,864,432, including monies held in the stabilization fund.

## **CURRENT AND PROJECTED REVENUE AND CASH ON HAND**

Historically, staff developed a recommended amount for distribution using two quarters of actual revenue and two quarters of projections, then adjusted to account for administrative costs and funds to be held in reserve. Last year, two unusual circumstances happened that impact our methodology for determining the amount for distribution for the upcoming grant year: (1) On March 1, 2008, the LSTFP implemented the IOLTA comparability statute; and (2) in 2008, the Federal Funds Target Rate (which is one indicator of bank rates) was reduced seven times, from a high in early January of 4.25% to a low in December of 0-0.25%. With implementation of the new comparability statute, April 2008 revenue was \$2.6 million (\$1 million more than April 2007): In December 2008, IOLTA revenue was \$1.24 million (\$350,000 less than December 2007).

The full impact of December cuts to the Federal Funds Rate will not be fully understood until mid-March 2009.

Due to the LSTFP's prudent reserve policy as well as implementation of the new comparability legislation, we are fortunate to have had a fund balance at June 2008 of \$20,520,566. However, while revenue for the 2008 calendar year came to over \$22 million -- nearly \$5 million more than 2007 -- rates have been dropping sharply and we now anticipate a deficit between revenue and expenses of \$2,785,502 at the end of the 2008-2009 grant year. To make matters worse, with the downturn in the interest rates and using what we hope to be a worst case scenario, IOLTA revenue may be as low as \$3 million per year for the next two fiscal years ended June 2010 and June 2011.

Because we know that the IOLTA-funded legal aid organizations are struggling with many funding cuts at a time when there are increasing numbers of people seeking their services, we are forced to make a hard decision. Assuming very low IOLTA yield for the next two years, should we push out as much funding as possible in 2009-2010 (10% cut in grants), even though that will leave little reserves for distribution in 2010-2011 (71% cut in grants), or should we try to even out the distribution of the grants over the next two years?

At the suggestion of the Commission, staff sought input from Trust Fund grantees through a survey that asked them to identify their preference as between getting a larger share of the funding now to allow them to serve the greatest number of people at the door, and time to put in place measures before the steeper cuts in year two, or more level funding to help them survive the second year of cuts. Although programs were divided between preferring Options 1 or 2, the programs that preferred Option 1 were fervent in their articulation of why they needed a larger distribution in the 2009-2010 grant year. To respond to the needs of the programs that preferred Option 2, staff made the further inquiry, "If the Commission were to develop a mechanism for your program to itself set aside a reserve for the 2010-2011 year, would that meet your needs?" The overwhelming majority of programs felt that pushing out maximum amounts of money now, but approving a temporary waiver of the Trust Fund Program's carry-over policy to allow grantees to create an internal reserve by carrying over as much as 50% of their grant award, is the best solution to meet the needs of all programs.

**PERSONNEL/BUDGET IMPLICATIONS:** This recommendation does not affect the general fund budget. No additional staff or other expenses will be incurred as a result of this recommendation.

**BOARD BOOK/ADMINISTRATIVE MANUAL IMPACT:** None.

**RULE AMENDMENTS:** No rule amendment is necessary.

## **RECOMMENDATION**

The attached schedule shows the calculation, based on actual experience through December 31, 2008 and projections through June 30, 2009; an allocation of funds from the Stabilization Reserve and projected 2008 donations to the Justice Gap Fund.

Because money will continue to be disbursed as it is received, the Trust Fund Commission will monitor revenue closely throughout the year and will return with recommendations if there are significant variances from the projections. The agreement signed with grant recipients includes language to make clear that distribution of grant funds is contingent upon the Legal Services Trust Fund Program having sufficient money on hand from IOLTA revenue to make the scheduled payments.

## **PROPOSED RESOLUTION**

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, 2009 through June 30, 2010 shall be made in the order and manner provided by Business and Professions Code Section 6216, and the funds to be distributed shall be \$13,968,403 calculated as follows:

- (1) The amount projected to be received by the Legal Services Trust Fund Program from July 1, 2009 through June 30, 2010, totaling \$3 million, shall be allocated for the grant period July 1, 2009 through June 30, 2010.
- (2) Funds from the reserve in the amount of \$11,718,403 shall be allocated for the grant period July 1, 2009 through June 30, 2010.
- (3) Donations to the Justice Gap Fund in the amount of \$750,000 shall be allocated for the grant period July 1, 2009 through June 30, 2010.
- (4) Projected administrative costs of \$1,500,000 for the period July 1, 2009 through June 30, 2010, shall be deducted.

**FURTHER RESOLVED** that grant payments are to be made from funds received pursuant to Business and Professions Code Section 6212, 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 Program is directed to monitor program revenue during the grant year, and to recommend changes to the grant amount, if necessitated by significant variances from projections.

State Bar of California  
 Legal Services Trust Fund Distribution  
 Available Funds for Grant Period 2009-2010 (Projected)

|   | <u>AMOUNT</u>                      |
|---|------------------------------------|
| A. Revenue - 07/01/08 - 06/30/09                            |                                    |
| 07/01/08 - 12/31/08 (Actual)                                | \$ 11,834,946                      |
| 01/01/09 - 06/30/09 (Projected)                             | 1,500,000                          |
| Interest Income   | 150,000                            |
| Justice Gap Funds (Projected 2009 Donations)                | <u>750,000</u>                     |
| Total Revenue:  | 14,234,946                         |
| <br>  |                                    |
| B. IOLTA Grant Distributions - 07/01/08 - 06/30/09          | 15,520,448                         |
| Admin 07/01/08 - 12/31/08 (Actual)                          | 770,235                            |
| Admin 01/01/09 - 06/30/09 (Projected)                       | <u>729,765</u>                     |
| Total Expenses:   | 17,020,448                         |
| <br>  |                                    |
| Net Projected IOLTA Revenue/Deficit 2008-2009:              | <u><u>(2,785,502)</u></u>          |
| <br>  |                                    |
| C. Reserves   |                                    |
| Reserve at 06/30/08   | 15,864,432                         |
| Cash on Hand at 6/30/08                                     | <u>4,656,134</u>                   |
|   | 20,520,566                         |
| Less Projected Deficit 2008-2009                            | <u>(2,785,502)</u>                 |
| Total Reserves:   | 17,735,064                         |
| <br>  |                                    |
| D. 2009-2010 Grant Calculation                              |                                    |
| Anticipated 2009-2010 IOLTA revenue                         | 3,000,000                          |
| Funds from Reserve  | 11,718,403                         |
| Anticipated 2009-2010 Justice Gap revenue                   | 750,000                            |
| Budgeted 2009-2010 Administrative expenses                  | <u>(1,500,000)</u>                 |
| <br>  |                                    |
| <b>Proposed 2009-2010 Distribution:</b>                     | <b>\$ <u><u>13,968,403</u></u></b> |
| <br>  |                                    |
| <b>Projected Fund Balance (Reserves) at June 30, 2010</b>   | <b>\$ 6,016,661</b>                |
| <b>% Change from 2008-2009 Distribution of \$15,520,448</b> | <b>-10.00%</b>                     |