

AGENDA ITEM

MARCH 161

DATE: February 9, 2011

TO: Members, Stakeholder Relations Committee
Members, Board of Governors

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

SUBJECT: Legal Services Trust Fund – Set Amounts for Distribution
2011-2012 IOLTA Grants, Justice Gap Fund and Temporary
Emergency Legal Services Fund

EXECUTIVE SUMMARY

Each year, the Board of Governors sets the grant amount available for distribution from Interest on Lawyers' Trust Accounts ("IOLTA"). Generally, the distribution amount is calculated by reviewing six months of actual IOLTA revenue and six months of projected revenue, less administrative costs. According to a policy recommended by the Legal Services Trust Fund Commission and adopted by the Board in 2006, a stabilization reserve fund was built during years when revenue was higher than the previous year, and for the last two years, this stabilization fund has been used to cushion the falling IOLTA revenue caused by the bad economy. Beginning in 2008, this distribution also included contributions to the Justice Gap Fund, and this year, for the first time, it includes funds from the new Temporary Emergency Legal Services Fund.

The IOLTA-funded nonprofit legal aid organizations continue to suffer the harsh effects of the down economy, while at the same time struggling to provide services for the increasing numbers of people needing civil legal aid. Therefore, this year, the Legal Services Trust Fund Commission again recommends that the Board of Governors approve maximizing the grant distribution through prudent distribution of amounts collected in prior years, at the same time recognizing the need to maintain 30% of the projected grant distribution for cash flow purposes and as a cushion against continuing low IOLTA revenue. The Commission recommends distributing \$10,685,829 in IOLTA, Justice Gap, and Temporary Emergency Legal Services Funds for the 2011-2012 grant year, leaving a projected fund balance at June 30, 2012 of \$3,377,779. The recommended IOLTA distribution reflects a 10% cut from the 2010-2011 IOLTA grant distribution, which in turn follows on prior year cuts of 15% and 10% in 2009-2010 and 2008-2009, respectively.

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 the amount of Interest on Lawyers' Trust Account (IOLTA) funds for distribution during the next 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; the legal aid organizations have 30 days to prepare proposed budgets; and, the staff and the commission can review the budgets, obtain fully executed grant agreements, and begin to distribute funds in July.

For each of the first eight grant years (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 1992, in response to low interest rates and declining revenue, the Board of Governors adopted the recommendations of the Trust Fund Commission and the Legal Aid Association of California (LAAC), to hold less than a year's cash on hand in order that more funds are immediately released for 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, that target was later reduced to 60% and then to 30%, where it remained for a 14-year period until 2006.

Revenue remained flat between 2001 and 2004 (below \$10 million), but showed steady increase in the years ended 2005 (\$11.6 million), 2006 (\$14.9 million), 2007 (\$17.1 million), and 2008 (\$20.2 million). For many legal aid organizations, IOLTA funding is a core support. Recognizing the importance of stabilizing grants to avoid big fluctuations in funding amounts, the Commission proposed revising the cash on hand policy to build a reserve that could be distributed during lean years. Then, as now, the Commission recognized that the ability to rely on stable IOLTA funding is critical to the health and survival of legal aid programs that are the beneficiaries of the statutory IOLTA framework. The Board of Governors approved that policy in 2006.

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 is applied whenever anticipated revenue exceeds prior

year grants: 1) the first 5% of any increase in revenue is distributed to legal aid programs; 2) the next 10% increase in revenue is held by the LSTFP in a stabilization reserve fund; and, 3) if projected revenue exceeds 15%, then the additional amount is divided equally between increased grants and increased reserve, up to a cap of 75% of the previous year's available funds.

CURRENT AND PROJECTED REVENUE AND STABILIZATION RESERVE

Historically, staff developed a recommended amount for distribution using two quarters of actual revenue and two quarters of projections, adjusted to account for administrative costs and funds to be held in reserve. This methodology worked well when interest rates fluctuated within normal market conditions, but was not a reliable predictor in 2008, when revenue increased substantially because of the newly enacted IOLTA comparability statute, or in 2009, when the federal funds target rate (which is one predictor of interest rates) dropped to the lowest in history.

In 2009, we reported that IOLTA-funded legal aid organizations were struggling with tremendous loss of funding at a time when there were increasing numbers of people seeking their services. Under that scenario, the Commission determined to push out as much funding as possible in 2009-2010 (10% cut in grants), even recognizing (and cautioning grant recipients) that if revenue did not outperform projections, there would be little reserve left to add to the grant distribution in 2010-2011. Fortunately, due to necessarily conservative projections, and the combined efforts of the Legal Services Trust Fund Commission, staff and the legal aid community to encourage banks to increase IOLTA rates, each year since 2009, we have been able to outperform IOLTA projections and those funds are reserved for distribution in the following year. This year, we are fortunate to have an additional projected \$1.5 million from the legislative Temporary Emergency Legal Services Fund. Because of these additional revenue sources, cuts for the 2011-2012 grant year need not be as steep as projected last year.

On January 31, 2011, the Commission met to review IOLTA and Justice Gap revenue and to arrive at a recommendation for distribution for this year. After an extensive review of projected revenue, and a discussion about the need for IOLTA programs to be able to rely on grant amounts allocated and to have monies to distribute next year, the Commission arrived at the recommendations below.

As detailed in the Projected Available Funds for Grant Period 2011-2012 (Attachment 1), the Commission requests that the Board approve a distribution of \$10,685,829 which represents a 10% drop in funding from last year. That amount is comprised of anticipated IOLTA revenue, funds taken from previous reserves, anticipated Justice Gap Fund contributions, investment income, and contract fees for administration of the Equal Access Fund grants, less the administrative expenses to operate the Legal Services Trust Fund Program. The grants will be distributed to the eligible programs under the statutory distribution formula. That will leave a projected fund balance of \$3,377,779 at June 30, 2012. Even if next year at this time we are able to project increased IOLTA revenue of \$7 million in

the 2012-2013 year, there remains a possibility of a 30% or more drop in grants for the 2012-2013 year.

Of course, this revenue projection is based on currently available information. We are keeping careful watch on the predictions of economists, who currently forecast that the Federal Reserve might raise the fed funds target rate in mid-2011, but that the State economy will remain in poor health deep into 2014.

FISCAL / PERSONNEL IMPACT:

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

RULE AMENDMENTS:

No rule amendment is necessary.

BOARD BOOK IMPACT:

None.

RECOMMENDATION

The attached schedule shows the calculation, based on actual experience through December 31, 2010 and revenue and expense projections through June 30, 2011.

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 BOARD COMMITTEE RESOLUTION:

Should the Stakeholder Relations Committee agree with the above recommendation, the following resolution would be appropriate:

RESOLVED, that the Stakeholder Relations Committee recommends that the Board approve that the distribution of IOLTA grants from the Legal Services Trust Fund Program for the grant period July 1, 2011 through June 30, 2012 shall be made in the order and manner provided by Business and Professions Code Section 6216, and the funds to be distributed shall be \$10,685,829 calculated as follows:

- (1) \$5.5 million from IOLTA revenue projected to be received by the Legal Services Trust Fund Program from July 2010 through June 2011;
- (2) \$4,045,829 from net assets/reserve;
- (3) \$2.25 million from total contributions on the member dues bill, including donations to the Justice Gap Fund in the amount of \$750,000, and contributions to the Temporary Emergency Fund in the amount of \$1.5 million;
- (4) \$350,000 in other revenue, including investment income and reimbursement for administration of the Equal Access Fund;
- (5) Less administrative costs, projected at \$1,460,000 for the period July 1, 2011 through June 30, 2012; and it is

FURTHER RESOLVED, that grant payments are to be made from funds received pursuant to California Business and Professions Code, Sections 6212 et seq. and Section 6033, and that payment of grants is contingent upon the State Bar having sufficient money on hand, after deducting for administrative costs, 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 between projected and actual revenue.

PROPOSED BOARD RESOLUTION:

Should the Board concur with the Stakeholder Relations Committee's recommendation, the following resolutions would be in order:

RESOLVED, that upon the recommendation of the Stakeholder Relations Committee, the Board hereby approves that the distribution of IOLTA grants from the Legal Services Trust Fund Program for the grant period July 1, 2011 through June 30, 2012 shall be made in the order and manner provided by Business and Professions Code Section 6216, and the funds to be distributed shall be \$10,685,829 calculated as follows:

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- (4) \$350,000 in other revenue, including investment income and reimbursement for administration of the Equal Access Fund;
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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 between projected and actual revenue.

Attachment 1 – Projected Available Funds for Grant Period 2011-2012