

## Potential Increase to Attorney Licensing Fee

### California Lawyers Association Fact Sheet

April 24, 2019

#### I. Current licensing fee

The current mandatory licensing fee for active attorneys is \$383. The amount of the licensing fee for inactive attorneys is different, but this fact sheet focuses on active attorneys.

The \$383 is calculated by adding different components and subtracting optional deductions, as set by statutes and other authority. The detail is shown below because some of the different statutory components are relevant to the State Bar's potential fee increase.

The licensing fee is currently calculated as follows:

#### 2019 Licensing Fee for Active Attorneys

- \$315 - Basic Fee (Bus. & Prof. Code § 6140)
- \$ 40 - Client Security Fund (Bus. & Prof. Code § 6140.55)
- \$ 25 - Discipline System (Bus. & Prof. Code § 6140.6)
- \$ 10 - Lawyer Assistance Program (Bus. & Prof. Code § 6140.9)
- \$ 40 - Legal Services Assistance (Bus. & Prof. Code § 6140.03)

TOTAL \$430

#### 2019 Optional Deductions

- \$ 5 - For attorneys who do not want to fund the State Bar's lobbying and other legislative activity. (Bus. & Prof. Code § 6140.05)
- \$ 2 - For attorneys who do not want to fund programs that address concerns of access and bias in the legal profession and the justice system. (*Keller v. State Bar of California* (1990) 496 U.S. 1)
- \$ 40 - For attorneys who do not want to fund legal services assistance. (Bus. & Prof. Code § 6140.03). This is the same \$40 shown above as part of the licensing fee, but the structure of including the amount and then providing for a deduction is statutorily mandated. Under Business and Professions Code section 6140.03, the State Bar is required to increase the annual licensing fee by \$40, to fund legal services, but the fee

statement is also required to provide each attorney with the option of deducting the \$40.

TOTAL    \$47

TOTAL MANDATORY FEE

\$430 - licensing fee  
- \$ 47 - optional deductions  
\$383

II.     Potential increase to the licensing fee

The State Bar has proposed three potential increases:

- An ongoing increase to the basic licensing fee
- A one-time special assessment for capital and technology investments
- A one-time increase in the amount paid for the Client Security Fund

At its meeting on March 15, 2019, the State Bar Board of Trustees authorized staff to pursue an ongoing licensing fee increase of up to \$100 plus an annual CPI adjustment; a one-time special assessment of up to \$250; and a one-time Client Security Fund assessment of up to \$80, effective January 1, 2020.

With the proposed increases, the 2020 Licensing Fee for Active Attorneys would be:

\$415 - Basic Fee (Bus. & Prof. Code § 6140)  
\$120 - Client Security Fund (Bus. & Prof. Code § 6140.55, \$40 plus \$80 one-time special assessment)  
\$ 25 - Discipline System (Bus. & Prof. Code § 6140.6)  
\$ 10 - Lawyer Assistance Program (Bus. & Prof. Code § 6140.9)  
\$ 40 - Legal Services Assistance (Bus. & Prof. Code § 6140.03)  
\$250 - special assessment for capital and technology investments

TOTAL    \$860  
- \$ 47 - optional deductions  
\$813

Separate from the State Bar's proposal, [Assembly Bill 1060](#) has been introduced. That legislation would make the \$40 fee increase for legal services assistance mandatory, removing the current statutory requirement that attorneys be provided with the option of deducting that \$40. The proposed State Bar increase, combined with this change,

would result in a 2020 licensing fee for active attorneys that would total \$853 (\$860 minus \$7 in optional deductions) and a licensing fee after 2020 that would total \$523 (\$530 minus \$7 in optional deductions), as it would not include the State Bar's proposed one-time assessments for 2020.

### III. State Bar Budget

#### A. Five-year forecast

The State Bar has completed a five-year forecast for its general fund, reflecting a comprehensive assessment of the State Bar's funding needs from 2020 to 2024. The five-year forecast presented at the Board of Trustees meeting on January 24, 2019 included the following key assumptions:

1. Mandatory licensing fee revenue to grow by 1.4% annually, resulting from projected growth in the number of licensed attorneys.
2. Rental Income to increase by \$1.5 million in 2020, which includes approximately \$0.9 million from leasing of floor three at 180 Howard St.
3. Personnel expenses, including:
  - a. An additional 58 positions in the Office of Chief Trial Counsel beginning in 2020 based on the State Bar's 2018 Workload Study and designed to ensure that the State Bar is able to meet statutory case processing timelines, estimated at \$7.8 million.
  - b. Per a negotiated labor agreement, SEIU salary adjustment of 3.5% in 2020, retroactive to 2019, estimated at \$2.7 million.
  - c. Providing parity for retiree health benefits for all employees (currently nonexecutive staff receive only \$133 per month in retiree health benefits, at most, while executive staff get between 80% and 100% of post-retiree health care costs covered after 15 years of service), increasing costs by \$3.2 million.
  - d. No other staffing increases.
4. Traditional ongoing expenses (utilities, maintenance, etc.) to grow at 3.0% annually.
5. New technology investments designed to increase transparency, public access, and customer service of \$16.0 million over five years, including

\$5.2 million in computer hardware & equipment and \$2.5 million on a new License Information Management System.

6. Implementation of a five-year capital plan addressing structurally under-funded and longstanding capital maintenance needs, with an investment of \$26.7 million.

At its meeting on March 15, 2019, the Board of Trustees was provided with an update on the State Bar's five-year forecast. That material is available here:

<https://board.calbar.ca.gov/docs/agendaitem/Public/agendaitem1000023891.pdf>.

The updated forecast reflected the following significant changes:

1. The change in mandatory fees was updated based on further demographic and admissions information, the new growth projection is 0.48 percent vs. 1.40 percent for active attorneys.
2. Rental income has been updated based on new leases and projected 3rd Floor lease revenue without costs for tenant improvements for the 3rd Floor.
3. Building improvement costs were updated as of February 7, 2019 based on deferred projects from 2019 to 2020.
4. Projected Retiree Health (OPEB) Costs are updated based on the new valuation as of March 2019.

The updated material reflects projected revenue and operating costs for the five-year forecast period and shows an ongoing deficit per the forecast of \$19.5 million in 2020 growing to \$33.3 million by 2024. As discussed below, the State Bar has identified a funding need based on the five-year forecast of:

1. \$100 average increase to the annual license fee for active licensees;
2. \$250 one-time special assessment for capital and technology investments, including reserves; and
3. \$80 one-time increase to the Client Security Fund fee

## B. 2019 Budget

The State Bar's Proposed 2019 Budget, as presented to the Board of Trustees in connection with approval of that budget, contains extensive financial details. That material is available here:

<https://board.calbar.ca.gov/docs/agendaitem/Public/agendaitem1000023538.pdf>

At its meeting on January 24, 2019, the Board of Trustees adopted a 2019 budget. Following that meeting, the State Bar issued a news release that contains a succinct summary of the 2019 budget and stated needs moving forward:

The Board of Trustees adopted a 2019 budget that projects \$168 in revenues and \$189 million in expenses. The budget reflects the State Bar's ongoing structural deficit, relying on reserve spending for the third year. The overall deficit in 2018 was \$22.5 million, less than originally projected because of efficiencies that saved millions of dollars, as well as a slight increase in projected revenues. The Board adopted a 2019 budget with reduced capital spending in 2019 to minimize impact on the Bar's significantly depleted General Fund reserve. The Board acknowledged that budget projections for 2020 and beyond demonstrate the unsustainability of the current trajectory, absent an increase in the attorney license fee, the chief source of the State Bar's General Fund revenue. The license fee of \$315 has remained unchanged for 20 years. Absent a fee increase in 2020, the Bar's budget deficit is projected to rise to approximately \$31.9 million, a situation that will require drastic cutbacks in State Bar operations and programs.... Without a fee increase, significant reductions in programs, staff, and capital/technology expense would be required no later than early 2021.

## C. 2020 Projected Budget

The State Bar is required to submit a two-year budget. As a result, in addition to the 2019 budget, the Board of Trustees was asked to adopt a 2020 projected budget for submission to the Legislature.

The 2020 projected budget, as adopted, does not reflect the State Bar's stated needs. Instead, it reflects a budget the Board of Trustees may have to adopt should a licensing fee increase not be approved for 2020. For the 2020 projected budget, the only significant forecast element is the full implementation of an SEIU salary adjustment of 3.5% in 2020, retroactive to 2019, which was negotiated in 2018. The 2020 projected budget, as adopted, includes reductions such as reductions in capital outlays. Even

with these reductions, there will be an approximately \$10.9 million deficit and reserves will end up at \$500,000 (which may cover only two days of operations).

#### IV. Ongoing increase to licensing fee

As noted above, the State Bar has identified a funding need of an ongoing \$100 increase to the licensing fee, with an annual CPI adjustment.

In a presentation given the day before the 2019 budget and 2020 projected budget were adopted, several key points were made, including the following:

- \$333 of the annual attorney licensing fee goes to the State Bar's general fund (\$315 basic fee, minus \$5 deduction for legislative activity and \$2 deduction for elimination of bias, plus \$25 for the discipline system). There has been no adjustment for inflation in this \$333 general fund portion of the licensing fee in over twenty years. If there were, that portion of the licensing fee would currently be \$519.
- The State Bar has run deficits for over three years. Not only is the projected deficit for 2019 \$10.4 million, but reserves will be down to \$11.5 million, which will cover only 6.6% of annual operating costs. The State Auditor has recommended that the State Bar have reserves in the amount of 17% of operating and the State Bar has set a target minimum reserve level of 17%.

#### V. One-time special assessment for capital and technology improvements

- Amount

As noted above, the State Bar has identified a funding need of a \$250 one-time special assessment for capital and technology improvements and investments.

- Stated needs and purpose

The funds would be used to address 1) structurally under-funded and longstanding capital maintenance needs; and 2) new technology investments "designed to increase transparency, public access, and customer service." The \$250 would specifically cover the following:

- \$128 for infrastructure improvements to HVAC systems, fire/life safety systems, elevators, and other structural issue.
- \$82 for technology improvements and upgrades

- \$40 in order to maintain a 17% reserve. (The State Bar has set a target minimum reserve level of 17%.)

## VI. Increase for Client Security Fund

The Client Security Fund (CSF) is funded by California attorneys, and was established as a way of reimbursing clients who have lost money or property due to theft or dishonesty by California attorneys. The CSF portion of the licensing fee is currently set at \$40 for active attorneys.

The State Bar was required to conduct a thorough analysis of CSF and submit a report on its analysis to the Legislature by March 15, 2018, so that the State Bar's plans could be "reviewed in conjunction with the bill that would authorize the imposition of the State Bar's license fee." (Bus. & Prof. Code § 6140.56(c)).

The full 2018 CSF report is available here:

<http://www.calbar.ca.gov/Portals/0/2018ClientSecurityFundReport.pdf>

- Amount

The State Bar has identified a funding need of an additional \$80 to the current \$40, resulting in a one-time increase of the CSF portion of the licensing fee to \$120.

- Stated needs and purpose

After 30 years of stability and timely reimbursements, with the onset of the loan modification crisis in the mid-2000s, applications by client/victims to the CSF, which totaled just under \$12 million in 2007, began growing steadily, eventually reaching \$50 million by 2012. The State Bar continued to fully reimburse victims, but payments have depleted the fund surplus. As of the date of the 2018 CSF report, CSF had an outstanding balance of applications currently eligible for payment totaling \$12 million, with an average time to payout of 3 years.

In order to consider the full array of options for addressing the challenges facing the CSF, the 2018 CSF report identified a number of options for consideration including:

- Initiatives that would provide additional resources to the CSF;
- Modification of executive and represented staff salaries; and
- One-time and on-going CSF fee increases.

The 2018 CSF report concludes:

While the Bar has endeavored to identify additional CSF resources over the last several years, it is clear that absent a significant one-time CSF fee increase these efforts will only have a marginal impact on the health of the Fund. Depending on the approach taken to address the CSF application backlog, the one-time amounts range from an *additional* \$5 to \$67 per licensed attorney. Further, in order to achieve the 12-month identified time to payout goal, a much more modest \$10 ongoing CSF fee increase is needed. Absent these needed increases, there is no way to address the fact that the demands on the Fund do not match its revenue and the ability to provide important reimbursements to victims is thus delayed and limited.

#### VIII. Fee scaling and hardship waivers

Active attorneys who can demonstrate “total gross annual individual income from all sources” of less than \$40,000 qualify for a waiver of 25 percent of the annual licensing fee. (Bus. & Prof. Code § 6141.1(b)). In addition to the legislatively required 25 percent waiver for those with income under \$40,000, State Bar rules afford fee waiver and scaling options. The State Bar provides for 25 percent scaling of licensee fees for attorneys who work at IOLTA-funded legal services organizations. State Bar Rule 2.16 (waivers) allows the State Bar secretary to waive 50 percent of the annual fee for licensees with household incomes below \$20,000.

At its March 15, 2019 meeting, the Board of Trustees was presented with the history and background of fee scaling and alternatives for scaling with the proposed fee increase, showing the increase to the licensing fee that would be needed from those above the fee scaling limits, in order to remain revenue neutral. That discussion begins on page five of the material available here:

<https://board.calbar.ca.gov/docs/agendaitem/Public/agendaitem1000023891.pdf>

The State Bar will continue to explore one or more scaling options to incorporate into the proposed fee increase methodology.

#### IX. Pending audits

The State Bar is currently subject to a financial audit every year and a performance audit every two years. The two audits are very different in purpose and scope. In 2019, the State Bar will be also be subject to an additional report by the Legislative Analyst’s Office (LAO). The two pending audits and LAO report are discussed below. As highlighted by the statutory language underlined below, the 2019 performance audit and

LAO report relate directly to any potential increase to the attorney licensing fee, and any such increase will ultimately be dependent upon the results of the audit and LAO report.

A. Financial audit

The State Bar is required to engage the services of an independent public accounting firm for an audit of its financial statement for each fiscal year. (Bus. & Prof. Code § 6145(a)). The *2017 Financial Statement and Independent Auditor's Report of the State Bar of California*, dated April 30, 2018, is available here:

<http://www.calbar.ca.gov/Portals/0/documents/reports/2017-Financial-Statement-and-Independent-Auditor's-Report.pdf>

The financial audit must be submitted within 120 days of the close of the fiscal year, so we should expect to see the 2018 audit by April 30, 2019. The external independent auditors review management and governance practices to ensure their compliance with all applicable standards, including those of the Governmental Accounting Standard Board (GASB) and the Financial Accounting Standards Board (FASB). As the 2017 report concludes:

This report is based on an audit conducted by an independent auditor for the purpose of forming opinions on the financial statements that collectively comprise the State Bar's financial statements as a whole. In the auditor's opinion, the State Bar's financial statements present fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

The financial audit is not an analysis of the State Bar's performance. The 2017 report did contain a discussion of the highlights of financial activities and the financial position of the State Bar, noting that this "analysis is designed to provide readers with information that the State Bar's management believes to be necessary to an understanding of its financial condition, changes in financial condition and results of operations." Among other things, the report noted the following economic factors facing the State Bar:

- The Supreme Court's directive that the State Bar require active licensed attorneys to resubmit fingerprints, resulting in a need for the State Bar to increase staffing to effectuate this requirement.
- The creation of CLA, separation of the Sections from the State Bar, and the associated financial impact.

B. Performance audit

Every two years, the State Bar is required to contract with the California State Auditor's Office to conduct a performance audit of the State Bar's operations for the respective fiscal year. (Bus. & Prof. Code § 6145(b)). In past years, the statute has not specified topics the audit should address, and those topics have varied. For the audit due in 2019, Business and Professions Code section 6145(c) added specific requirements, as follows:

(c) (1) For the 2019 audit required pursuant to subdivision (b), the California State Auditor's Office shall conduct a performance audit of the State Bar as set forth in this subdivision. The State Bar shall provide technical assistance, data, or information as requested by the California State Auditor. It is the intent of the Legislature that this audit can be reviewed in conjunction with the legislation that authorizes the State Bar's licensing fee in 2020.

(2) The audit shall evaluate each program or division of the State Bar receiving support from the annual State Bar licensing fees and other fees required of active and inactive licensees.

(3) The audit shall, at minimum, include the following for each program or division:

(A) An assessment of how much fee revenue, staff, and resources are currently budgeted and subsequently expended to perform existing tasks and responsibilities.

(B) An assessment of whether the State Bar has appropriate program performance measures in place and how these measures are used for budgeting purposes.

(C) An assessment of the usage of real property owned by the State Bar.

(D) A review of the State Bar's cost allocation plan used to allocate administrative costs.

(E) A review of any proposals for additional funding or resources requested by the State Bar to determine whether these proposals are necessary to meet the State Bar's public protection function, as well as the accuracy of identified associated funding needs, after reviewing how existing resources are used.

(F) A calculation of how much fee revenue would be needed from each State Bar active and inactive licensee to fully offset State Bar costs to perform existing tasks and responsibilities and to support additional proposed expenditures determined to be necessary to meet the State Bar's public protection function. This calculation shall take into account any proposed business process reengineering, reallocations, or efficiencies identified by the California State Auditor.

The 2019 performance audit must be submitted by May 1, 2019 to the State Bar's Board of Trustees, the Chief Justice, and the Assembly and Senate Judiciary Committees, but the public report may follow. In past years, the final report has included the audit results, the State Bar's response, and the State Auditor's comments on the State Bar's response.

The full 2017 State Auditor's report is dated June 27, 2017, and is available here: <https://www.auditor.ca.gov/pdfs/reports/2017-030.pdf>

The full 2015 State Auditor's report is dated June 18, 2015 and is available here: <https://www.auditor.ca.gov/pdfs/reports/2015-030.pdf>

### C. LAO Report

In 2019, for each program or division assessed by the State Auditor in accordance Business and Professions Code section 6145(c)(2) – as listed above – the Legislative Analyst's Office is required to "assess whether the State Bar effectively utilizes licensing fee revenues to maximize efficiencies." (Bus. & Prof. Code § 6145(c)). The LAO is required to submit this report to the Legislature and the Chief Justice by July 1, 2019.

By way of general background, the LAO has provided fiscal and policy advice to the Legislature for 75 years. Historically, one of the most important responsibilities of the LAO has been to analyze the annual Governor's budget. More generally, the office is a staff resource to all legislators. The LAO also performs the following functions:

- Budget "Control." The LAO reviews requests by the administration to make changes to the budget after it is enacted.
- Special Reports. Throughout the year, the office prepares special reports on the state budget and topics of interest to the Legislature.
- Initiatives and Ballot Measures. The office estimates the fiscal effect on state and local government of all proposed initiatives (prior to circulation) and prepares analyses of all measures that qualify for the statewide ballot.