

REPORT OF THE
OFFICE OF THE AUDITOR GENERAL
TO THE
JOINT LEGISLATIVE AUDIT COMMITTEE

284.1

REVIEW OF THE STATE BAR
OF CALIFORNIA

AUGUST 1976



Joint Legislative Audit Committee

OFFICE OF THE AUDITOR GENERAL

California Legislature



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August 13, 1976

The Honorable Speaker of the Assembly
The Honorable President pro Tempore of
the Senate
The Honorable Members of the Senate and the
Assembly of the Legislature of California

Members of the Legislature:

Your Joint Legislative Audit Committee respectfully submits the Auditor General's report on the accounts and internal fiscal planning of the State Bar of California.

As reported by the Auditor General in a 1974 study, the governing body of the State Bar has not yet fully developed workload standards upon which to make a satisfactory analysis of projected staffing needs.

The Board of Governors has concluded that its almost 50,000 members should be assessed an additional \$1.3 million annually for staffing needs.

In the judgment of the Auditor General, the projected budget of the Bar Governors can be supported without the \$1.3 million assessment and with a \$251,000 year-end balance on December 31, 1977.

The auditors are Robert Neves, Manager; David Tacy and Alan Kalin.

Cordially,

MIKE CULLEN
Chairman

MC:p11

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SUMMARY

The California State Bar has grown significantly in recent years, and it is requesting the Legislature to authorize a \$1,300,000 increase in 1977 membership fees charged to active California attorneys.

In 1974, we recommended that the Legislature disapprove a similar fee increase proposal on the grounds that the State Bar had not prepared a specific written analysis of its cost projections. Our current review indicates the State Bar has yet to recognize the need to properly plan or account for proposed budget increases. The State Bar has not sufficiently documented or allocated its proposed 1977 expenditures so that an independent evaluation of the need for the proposed expenditures can be made.

Our review also disclosed that except for a temporary cash shortage in one month, the State Bar could finance all of its proposed 1977 expenditures from its own cash resources. We project that a 30- to 45-day \$200,000 loan will be necessary to carry the Bar in November 1977 until December, when advance fees receipts will permit loan repayment. If the Legislature wishes to permit the Bar to finance all of its proposed 1977 expenditures, we recommend that the Legislature amend the Business and Professions Code to permit the Bar to borrow from otherwise inaccessible resources within the Bar.

INTRODUCTION

Purpose and Scope of Review

In response to a legislative request, we are reviewing the State Bar of California's compliance with our 1974 recommendations.^{1/}

In brief, the Auditor General recommended:

1. That the Legislature disapprove proposed increases in State Bar membership fees until the State Bar developed sufficient justification for those increases,
2. That the State Bar make efficient use of its facilities before constructing new ones, and
3. That the State Bar substitute administrative assistants for attorneys whose duties at the State Bar did not require their legal expertise.

To be most responsive to legislative needs, we divided the current review into two reports. This first report addresses the State Bar's justification for proposed fee increases which the Legislature is being asked to approve for 1977. A second report will address the State Bar's compliance with our other two 1974 recommendations and the significant management issues our current review has disclosed.

^{1/} Reports of the Auditor General to the Joint Legislative Audit Committee (223.1 and 223.2), Subject: State Bar of California.

Background

The State Constitution requires that every attorney licensed in California be a member of the State Bar except for active judges of a court of record. The powers, duties and organization of the State Bar are specified in Section 6000, et seq. of the Business and Professions Code.

The State Bar's primary function is to regulate the legal profession in California. Under the jurisdiction of the State Supreme Court, the State Bar conducts the examination and licensing of attorneys, and the investigation and censure of members accused of professional misconduct. In appropriate cases, the State Bar may recommend that the State Supreme Court suspend or disbar a member. In addition, the State Bar may pay up to \$25,000 of special memberdues to each member's client who suffers pecuniary loss because of that member's professional misconduct.

In addition to these regulatory activities, the State Bar represents the interests of the legal profession before the Legislature and the public. The Bar makes recommendations regarding the Governor's judicial appointments and the administration of justice. As California's professional attorney association, the State Bar also conducts an annual convention, publishes a monthly bulletin The State Bar of California Reports: and a bimonthly California State Bar Journal, and supervises a continuing professional education program operated by the University of California.

The State Bar is governed by a 15-member Board of Governors elected from various geographical districts. Five governors are elected each year to three-year terms, for which the governors receive no remuneration. At the beginning of the Board's next term, the Board is to be composed of 21 members; the six new members are to be nonlawyers appointed by the Governor. The Board selects its own officers each year and appoints a secretary who serves as the executive director.

As of June 9, 1976, the State Bar had an active membership of 49,527 attorneys. In 1976, projected membership and examination fees should provide \$5,500,000 of the Bar's expected revenues of \$5,900,000. A full-time staff of 198 is budgeted for State Bar activities in 1976. Staff work is supplemented by voluntary service from State Bar members.

Significant Membership Fee Increases Requested

The State Bar has requested the Legislature for authority to increase 1977 membership fees the equivalent of \$1,300,000. This represents 32 percent more revenue than would be generated from the current rates. (Natural growth in membership would increase membership fee revenues \$284,000 without a fee increase.) As the following table indicates, these proposed increases represent an acceleration of already significant increases made since our review in 1974. The State Bar currently charges the maximum fees authorized by the Legislature effective January 1, 1976.

Table 1

Profile of State Bar
Membership Fees and
Related Revenue
1974-1977

	<u>1974</u>	<u>1976</u>	<u>Proposed 1977</u>
Membership Fees for Active Attorneys Admitted:			
0 - 2 years	\$45	\$50	\$ 55
2 - 5 years	60	70	85
5 - 10 years	80	90	115
over 10 years	80	90	130
State Bar Membership:			
Total	40,700	49,500*	52,900*
Percent of 1974	100%	122%	130%
Total Membership Fee Revenues:			
Total	\$3,000,000	\$3,900,000*	\$5,600,000*
Percent of 1974	100%	133%	187%

*Estimates

If the State Bar charges its proposed 1977 membership fees, membership fee revenues will have increased 87 percent in three years.

FINDINGS

THE STATE BAR HAS NOT PREPARED
SUFFICIENT DOCUMENTATION FOR
PROJECTED 1977 EXPENDITURES TO
WARRANT PROPOSED MEMBERSHIP
FEE INCREASES.

The State Bar has requested the Legislature for authority to increase 1977 membership fees. However, the State Bar's 1977 expenditure projections were prepared without sufficient documentation and planning to warrant the proposed fee increases. The State Bar has also not prepared a specific written analysis of workload standards and statistics recommended by the Auditor General in 1974. As a result, an independent determination of the need for most of the State Bar's proposed 1977 expenditures cannot be made.

The State Bar's proposed membership fee revenue is intended to cover expenses in all programs except certain self-supporting activities (Bar Examinations, Legal Specialization, and Sections). The State Bar also proposes to use the 1977 revenue to offset its projected 1976 accounting deficit. Table 2 provides an overview of the Bar's projected 1977 budget.

Table 2

California State Bar
Projected 1977 Budget

1976 Budget (Excluding certain self-supporting activities)		\$4,596,000
Proposed Increases for 1977:		
New personnel (33 positions)	\$366,000	
8% merit increase to existing positions	209,000	
Employee benefits	97,000	
Operating expenses	<u>209,000</u>	
Total Proposed Increases		881,000
Elimination of 1976 Accounting Deficit:		
Per Bar Proposal (Appendix B)	350,000	
1976 Budget Augmentation	<u>82,000</u>	<u>432,000</u>
Proposed Budget for 1977 (Excluding certain self-supporting activities)		5,909,000
Projected Budgets for Certain Self-Supporting Activities:		
Bar Examinations		1,588,000
Legal Specialization and Sections		<u>145,000</u>
Total Projected Budget for 1977		<u>\$7,642,000</u>

Failure to Develop Workload Standards

With the exception of two departments (Disciplinary Enforcement and General Counsel), the State Bar has not complied with the Auditor

General's recommendation in June 1974 that "...a specific written analysis of staffing needs based on workload statistics and standards" be developed. Workload standards are applicable to most State Bar activities. Appendix A outlines some concepts of such standards and how they might be applied to State Bar activities.

In their review of state agency budgets the Department of Finance and the Legislative Analyst consider workload standards wherever appropriate. The Legislative Analyst relies heavily on staff projections based on such standards. In addition, both of these fiscal review offices require specific written analyses of each proposed program expansion or other expenditure increase. The State Bar is not subject to regular reviews of the nature described and has not developed the kinds of data required of state agencies to justify their budgets.

Unsubstantiated 1977 Expenditure Projections

The only analysis of proposed 1977 expenditures provided by the State Bar for our review is attached as Appendix B. The June 1976 State Bar Reports also discussed the proposed expenditures; a copy of that article is attached as Appendix C. With the exception noted in the following paragraph, neither analysis allocated proposed expenditures among the various State Bar departments. Without information on how the Bar intends to distribute funds among its departments, independent analysis of the need for proposed expenditures cannot be made.

The State Bar has allocated 33 proposed positions to 12 departments. Even without workload standards for measurement, some of the 1977 proposed staff increases are not representative of identifiable needs. When questioned, supervisors in some departments were unable to justify the projected staff additions. The efficiency of work in two departments (Membership Records and the Print Shop) is being re-evaluated to the extent that staff increases are premature. Three other departments (Legal Services, Grant Programs, and Committee Assistance) have not been provided sufficient guidance by the Board of Governors so that department staff can plan resource needs accurately. We conclude that of the 33 proposed staff additions, which represent the only expense category allocated to departments, at least 12 of those positions are unneeded or premature.

Workload standards developed by the General Counsel and Disciplinary Enforcement Departments (including Investigators) appear to justify 13 of the 15 projected staff increases for those two departments. The other two staff positions are for a proposed experiment to shift some workload from attorneys to less expensive paraprofessional staff.

Need for Improved Planning

We believe the Bar's failure to document and justify its proposed 1977 expenditures is part of a larger deficiency in fiscal planning. Formal planning for 1977 departmental expenditures will not begin until August 1976 for budget adoption by early January 1977. Therefore, the State Bar has requested legislative approval for a fee increase

prior to the Bar's only specific planning and budgeting process. At present, the only formal long-range planning is being conducted by a recently created State Bar Special Committee to Study the Role of the State Bar.

In our opinion, the Bar's planning capability would be significantly enhanced by more specific direction and advance decision making by the Board of Governors. Until the Board formally commits itself to a ranking of program priorities and a timetable of specific program objectives, the staff cannot effectively project resource requirements. Ranking priorities and projecting costs must occur sufficiently in advance of identifiable fiscal problems to permit appropriate remedial action, whether to lower expectations or to request fee increases.

The State Bar has made progress in improving its management in other areas since our 1974 review. A new computerized accounting and financial information system provides detailed cost information necessary to fiscal planning. A personnel compensation plan that was adopted should facilitate improved hiring and promotion practices. Studies have also been undertaken to examine the efficiency of selected operations. These measures are positive steps toward improved management.

Even so, the Secretary of the State Bar agrees that the Bar needs to improve its formal fiscal planning. We believe that the key to the Bar's planning success will be the commitment the Board of Governors makes toward setting program priorities and developing systematic fiscal projections.

CONCLUSION

To a great extent, the State Bar has not complied with our 1974 recommendation that workload standards be developed. As a result of this and inadequate planning and documentation, the State Bar has not sufficiently justified its proposed 1977 expenditures to warrant the requested increase in membership fees.

RECOMMENDATIONS

The State Bar should develop a formal procedure of fiscal planning.

Prior to requesting legislative approval for membership fee increases, the State Bar should prepare a specific written analysis of its priorities, plans and cost estimates for each program's development in the projection period. Where appropriate, such an analysis should include quantified projections of workload and the resources needed to service it.

BENEFITS

Implementation of these recommendations will improve the State Bar's ability to develop meaningful data upon which objective decisions can be made.

THE STATE BAR DOES NOT NEED A FEE
INCREASE TO FINANCE ALL PROPOSED
1977 EXPENDITURES.

Late in the year, the State Bar receives substantial membership and bar examination revenues due in the early months of the next year. For example, as of December 31, 1975, the Bar had received in excess of \$1,000,000 of 1976 fees. There is every reason to believe that this trend will continue. As a result, we project that the State Bar could finance all proposed 1977 expenditures and end the year with about a \$251,000 cash balance. However, in order to finance all of the Bar's proposed expenditures, a temporary cash loan of about \$200,000 will be needed in November 1977, until the advance fee payments are received in December when the loan would be repaid. This loan would allow the State Bar to cover all proposed expenditures without a 1977 membership fee increase.

Appendix D summarizes the major assumptions made and the character of the work we performed in developing the cash requirements forecast supporting our conclusions.

Substantial Cash Income from Fees Paid in Advance

The State Bar normally receives a substantial portion of its next-year membership and Bar examination fees in the current year. The significance of the amount has depended on when the State Bar has mailed its membership billings. The State Bar has used these receipts to pay current-year expenses in two of the last four years.

By utilizing receipts in this manner, we project that without a 1977 membership fee increase the State Bar's December 31, 1976 ending cash balance could amount to about \$716,000 and that 1977 cash receipts will total \$6,480,000.

Delay in Deposits of Bar Examination Receipts

The State Bar's cash projections do not reflect all cash to be received from Bar examination fees. State Bar records indicate that up to four months elapsed between receipt of such fees in November and December 1975 and their deposit in State Bar bank accounts. If Bar examination fees are deposited in a timely fashion, we project that 1977 cash flow could be increased by another \$265,000.

Projected 1977 Cash Flow

The following table outlines our projections of the State Bar's cash position in 1977 and shows that the Bar's projected expenditures can be absorbed by the existing fee structure.

Table 3

Projected 1977 Cash Flow (See Note 1)
(Assuming No Fee Increase)

Projected Cash Balance, December 31, 1976		\$ 716,000
Projected Cash Receipts in 1977 without Improvement in Bar Exam Fees Depositing		6,480,000
Projected 1977 Effect of Improved Bar Exam Fees Depositing		<u>265,000</u>
Total Cash Available in 1977		7,461,000
Proposed 1977 Expenses (Including 1976 Deficit)	\$7,642,000	
Less Adjustment for 1976 Accounting Deficit Not Requiring Application of 1977 Cash	<u>432,000</u>	
Cash Expenditures for 1977		<u>7,210,000</u>
Projected Cash Balance, December 31, 1977		<u>\$ 251,000</u>

Note 1: Refer to Appendix D for a summarization of the underlying assumptions and cautions relating to cash forecasts.

Inappropriate State Bar Revenue Projections

The State Bar has reported to its members that without a fee increase it will have an accounting deficit of \$1,600,000 as of December 31, 1977. However, because of the fees collected in advance, our analysis shows the State Bar may pay all proposed expenditures and have a cash balance of about \$251,000 as of December 31, 1977. The apparent discrepancy between our analysis and the Bar's results from the fact that there is usually little relationship between an accounting deficit and cash balances in accrual accounting procedures followed by the State Bar. At the State Bar, an accounting deficit may occur in December because unpaid creditor bills are properly recorded as accrued expenses in the current year, and cash received in December as next year's membership fees is properly recorded as revenue to the following year. Nevertheless, the cash from advance fees can be on hand in December, but the cash for accrued expenses will not yet have been disbursed. Therefore, the Bar's cash position can be positive even if accounting records show a "paper" deficit. For purposes of projecting the operating needs of the State Bar, cash flow and not accounting income is the relevant consideration.

Insufficient Cash Projected to Cover
Proposed November 1977 Expenses

We project that without a fee increase the State Bar could end 1977 with about a \$251,000 cash balance after all proposed expenditures. However, cash requirements in November 1977 could require a temporary

loan of about \$200,000 for that month. Such a loan might be acquired from other State Bar funds, from the state treasury, or from commercial sources. The following analysis discusses each alternative's relative merits.

The State Bar has substantial cash balances in its Client Security and Building Funds, each of which is supported by a \$10 annual fee from each active member. The Building Fund will probably be needed to finance construction under way on the Bar's \$5,600,000 addition to its San Francisco headquarters. However, claims against the Client Security Fund have been only a fraction of the fund balance, and we believe the Client Security Fund could finance a 30- to 45-day loan to the Bar's General Fund at the lowest cost of any of the loan alternatives. However, a Legislative Counsel opinion indicates that this is legally prohibited as outside the Client Security Fund's purposes, as defined in Section 6140.5 of the Business and Professions Code. Legislative amendment of this section would be necessary for the Bar to use this least-cost loan source to aid in financing its proposed 1977 expenditures.

The second alternative is to borrow from the state treasury. This too may require legislative action and could cost the Bar more in loan interest than just the foregone interest income on \$200,000 of the Client Security Fund.

A third alternative would be commercial borrowing. Although the Bar already has legal authority to borrow, this would probably be

the most expensive of the three alternatives. We conclude that the best alternative to aid in financing all of the Bar's proposed 1977 expenditures would be legislative action to permit the Bar to temporarily borrow \$200,000 in 1977 from its Client Security Fund.

Future Implications of Cash Management in 1977

If the State Bar finances its proposed 1977 expenditures through improved cash management and minor temporary borrowing, it may not be able to perpetuate such an expenditure level without increasing membership fees in 1978. We believe that the suggested 1977 cash management program will provide the State Bar with an opportunity to prepare adequate justification for a 1978 membership fee increase which may be necessary.

On the other hand, if the State Bar charges its proposed 1977 membership fees, we project an ending 1977 cash balance of about \$1,600,000. This includes approximately \$58,000 in additional interest income that would be earned if the fee increase is granted. The Bar has not justified the need for such cash reserves, which would exceed the increased revenue projected from the proposed fee increases.

CONCLUSION

The State Bar, subject to the assumptions in Appendix D, can finance all of its proposed 1977 expenditures from projected cash flow without increasing membership fees. However, we project that a temporary loan of about \$200,000 could be needed in November 1977 to fully finance all proposed 1977 expenditures.

RECOMMENDATIONS

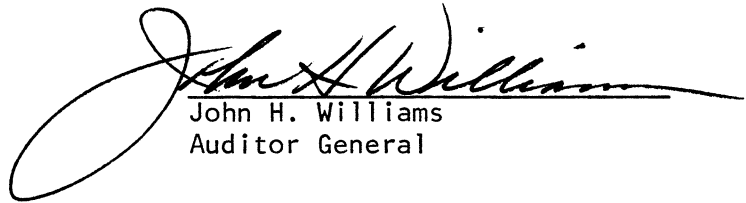
We recommend:

- The Legislature should not authorize the State Bar to increase its membership fees in 1977.
- If the Legislature wishes to permit the State Bar to finance all proposed expenditures in 1977 as we have described, the Legislature should amend Section 6140.5 of the Business and Professions Code to permit the State Bar's General Fund to temporarily borrow about \$200,000 from the Client Security Fund in 1977.
- The State Bar should incorporate cash flow analysis into its projections of revenue needs before requesting legislative approval of membership fee increases.

BENEFITS

In 1977, the State Bar membership will save \$1,300,000 in membership fees, or an average of \$24.57 for each of the projected 52,900 active members.

Respectfully submitted,



John H. Williams
Auditor General

August 10, 1976

Staff: Robert M. Neves
David Tacy
Al Kalin



THE STATE BAR OF CALIFORNIA

Office of the Legislative Representative

1210 K STREET

SACRAMENTO, CALIFORNIA 95814

TELEPHONE (916) 444-2762

August 10, 1976

Mr. John H. Williams
Auditor General
State of California
925 L Street, Suite 750
Sacramento, Ca. 95814

Dear Mr. Williams:

We are appreciative of the effort expended and the content of the August 1976 Auditor General's draft review of the State Bar of California.

We respectfully disagree with the Auditor General's conclusions. In fact, we believe that the Auditor General's Report when properly analyzed and evaluated will support the State Bar's position that the Legislature should authorize the State Bar to increase membership fees for the calendar year 1977.

We will demonstrate with brevity the reasons for our conclusions in this regard.

Initially, we emphasize the fact that the State Bar does not seek revenue from the State's General Fund. Rather the Bar seeks legislative authorization to increase for one calendar year, only 1977, the fees of members of the State Bar so that it can operate on a fiscally sound "pay-as-you-go" basis.

In stark contrast to this fiscal philosophy is the recommendation of the Auditor General's Report which suggests a deficit financing plan. The result of this would only serve to defer the inevitable. In our opinion the end result would be serious impairment of the efficient and prudent operation of the State Bar.

The gist of the Auditor General's Report and its conclusions are as follows:

- (1) To a great extent the State Bar has not complied with the Auditor General's 1974 recommendations that workload standards be developed.
- (2) As a result of this, the State Bar has not justified the proposed increase in 1977 expenditures so as to warrant the requested increase in membership fees.

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- (3) If the projected "cash flow" for 1977 is examined, there is no need to increase the fees; rather, the Legislature need only amend the State Bar's General Fund to permit the borrowing of \$200,000 from the Client Security Fund to accommodate a shortage which may occur in November of 1977.
- (4) A 1978 membership fee increase "may" be necessary.

We discuss these conclusions in order to point out their questionable validity.

1. Workload Standards

An analysis of the Auditor General's own Report demonstrates that the State Bar has not failed to comply with the Auditor General's 1974 recommendations to develop workload standards.

Actually the Report does reveal on its face and by obvious deduction and personal observation that almost 96 percent of the proposed 1977 State Bar budget* is justified by (i) items conceded in the Report to reflect appropriate workload standards, or (ii) items to which workload standards have no relevance, or (iii) items, the justification for which are apparent even without application of any workload standards.

In the first place, the Report concedes that in two departments, Disciplinary Enforcement and General Counsel, the State Bar has developed workload standards. (see page 6 of Report). The Report fails to point out that the projected cash requirements for these two departments is approximately 1.9 million dollars. This constitutes roughly 33 percent of the proposed 1977 budget.

In the second place, at least 20 percent of the proposed 1977 budget of the State Bar (an amount in excess of \$1,000,000) represents items with respect to which workload statistics have little relevance. For example, rent, repair and maintenance, utilities, insurance, telephone, and the like.

In the third place, the Auditor General's Report recognizes that some portion of activity may not be amenable to workload "unit" analysis. Although the Auditor's General's Report is the result of some three months observation of the State Bar operation, nevertheless, it nowhere indicates what any reasonable man approach would readily discover -- that a good portion of the support activities for the operation of

*When we refer to the proposed 1977 budget, we refer only to those matters totaling 5.6 million dollars supported by membership fees as distinguished from other self-supporting activities such as the Bar Examination, Specialization, etc.

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the State Bar would require significant expenditures regardless of the existence of any workload unit standards. In our opinion, an appraisal of expenditures for the year 1977 for these needed support activities totals at least \$2,500,000. This constitutes approximately 43 percent of the proposed 1977 budget.

In short, the foregoing analysis demonstrates that approximately 96 percent of the entire proposed 1977 State Bar budget is justified from either the Report itself or what we believe should have been apparent from the Auditor General's study of the Bar operation.

2. Justification of Proposed Fee Increase

We submit that a fair analysis of the material referred to in the preceding section amply supports the position of the State Bar that the requested fee increase is necessary in the prudent management of the State Bar's affairs with which the Board of Governors is charged.

We further point out that the Auditor General's Report does not criticize the expenditure level at the time the Report was written. The Auditor General agreed, and informed us, late Friday afternoon, August 6, 1976, that in this respect the Report would only be directed to the increase of expenses for 1977 over the current expenditure level.

As is shown elsewhere in the Report, we maintain that the proposed 1977 increase of \$881,000 is fully justified. Even using the Auditor General's criteria with which we do not agree and adding thereto normal increases and required contractual obligations, there would have to be an increase, on a most conservative basis, of at least some \$637,000. The items involved are: \$234,000 based on the cost of only those personnel which the Report admits is justified; normal increases of \$208,000 to present employees; increases of \$78,000 required by contractual obligations under health benefit and pension plans; and \$117,000 resulting from the inflationary affect on fixed operating expenses.

Such a controverted deficiency of some \$245,000 hardly suggests that the proposed fee increase lacks adequate justification.

3. The Auditor General Staff's Proposed "Cash Flow" Financing

We submit that thus far we have seen that the Auditor General's Report itself contains a two-fold justification for the 1977 State Bar budget.

First, from the Report's contents and from what was readily observable by the staff of the Auditor General during the course of its three-month study of the State Bar operation, the proposed 1977 State Bar budget is justified (See point 2 above).

Second, the increase of some \$881,000 in the proposed 1977 State Bar budget over the 1976 expenditures is not as the Report suggests "largely unjustified." (Page 1 of Report). Rather, it too is justified by a combination of factors: (a) the admittedly justified increase in cost of Discipline Enforcement and operation of the General Counsel's office; (b) the increase in cost attributable to the support staff for the administration of the disciplinary process; (c) an inflationary factor which must be accepted and not ignored;

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August 10, 1976

(d) the inclusion of a contingency allowance for unbudgeted items which, although not foreseen at any given moment, almost inevitably occur; and (e) the cost of the admittedly justified increase in personnel for 1977.

Even if all of the foregoing were not so, we believe that sound financial planning calls for the rejection of the recommendations made by the staff of the Auditor General for financing the 1977 operation of the State Bar.

In effect, the Auditor General's plan is to tide the Bar over 1977 by:

- (a) Using 1977 fees which members conceivably may pre-pay toward the end of 1976, and
- (b) Seeking enabling legislation which permits the State Bar to borrow "temporarily" over \$200,000 from the Client Security Fund, and
- (c) Postponing legislative authorization for an increase of fees until 1978.

Contrast this "rob Peter to pay Paul" deficit financing approach with the "pay-as-you-go approach" which the State Bar proposes that the Legislature authorize for 1977.

We do not rely as does the Auditor General's staff, on pre-payment which may not occur, the amount of which is not assured, and the amount of which in fact has at times been very little. But whether small or large it should be noted that pre-paid sums are not a "cash reserve" (See page 15 of Report). Rather they are funds which are in effect ear-marked for expenditure during the year 1977.

We do not suggest as does the Auditor General's staff, that the Legislature allow the State Bar to dip, even temporarily or ever so slightly, into the Client Security Fund, a fund created by annual \$10 contributions by each member of the Bar and held for the protection of the public against any defalcations.

We earnestly recommend that inasmuch as a need will, without doubt, be present no later than 1978, then the year 1977 is not too early to start providing for this need by permitting an increase in membership fees.

We suggest that the Client Security Fund remain intact, grow by interest accumulations, and that its present size may well permit a one year moratorium on contributions.

We propose a "pay-as-you-go plan" rather than a deficit financing plan. The State Bar plan places the bulk of the proposed fee in-

Mr. John H. Williams, Auditor General

August 10, 1976

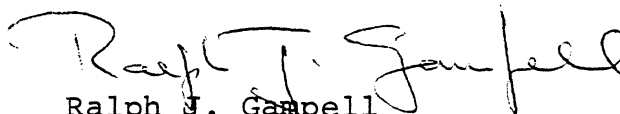
crease on the members of the Bar best able to afford it. Here is the net effect if the proposed enabling legislation on membership fees for the year 1977 is enacted:

Years of Practice	Present Fees	Proposed Fee Limits for Year 1977	Net 1977 Fees*
0 - 2	\$50	\$55	\$45
2 - 5	70	85	75
5 - 10	90	115	105
over 10	90	130	120


*(Takes into account possibility of one-year moratorium on Client Security Fund contributions of \$10 per member.)

Finally, we make no demands for any State funds. We seek only legislative authorization for a fee increase. And we seek this authorization for only one year, 1977.

Respectfully,



Ralph J. Gampell
President-Elect



Edward Rubin
Treasurer-Elect

b

STATEMENT BY THE AUDITOR GENERAL
IN RESPONSE TO THE STATE BAR'S COMMENTS

The State Bar's comments on the justification of proposed 1977 expenditures reiterate our report to the extent that staff increases in two departments appeared to be justified on the basis of workload standards. However, the Bar's comments did not note that we could not determine the need for any other proposed expenses of any departments because the Bar had failed to allocate proposed expenses among departments. We agree with the Bar that a reasonable man might conclude that proposed expenditures were necessary if he knew how all of those expenses would be distributed. The State Bar's suggestion that at least 96 percent of proposed 1977 expenditures are justified cannot be verified without such an allocation of expenses among departments. Such an allocation has not been provided to us by the State Bar.

The State Bar is correct that our proposed cash management "robs Peter to pay Paul" in the sense that the Bar should use virtually guaranteed income to finance proposed expenses. However, it is incorrect to characterize this proposal as risky or expensive. The small risk is attested by the Bar's history of such financing, which the Bar intends to employ again in 1976 to provide cash in December for an expected \$432,000 accounting deficit. Further, unlike "deficit financing", our proposal entails no borrowing cost, except for a slight reduction in interest income.

We believe the central issue in our analysis of the Bar's cash flow is whether the Bar should take full advantage of its cash resources or whether a significant cash reserve should continue to be accumulated. We propose that the State Bar draw down its cash balances in 1977 to save the membership \$1.3 million. We believe utilizing cash as it is received is the essence of the "pay-as-you-go" principle the Bar recommends.

Page 4 of the Bar's comments states that "the year 1977 is not too early to start providing for this need (for more funds in 1978) by permitting an increase in (1977) membership fees." It is clear to us that the Bar recognizes 1978 as the year of need and not 1977. Our position is that the Bar should utilize available resources until the need arises.

It should also be noted that the table of proposed fees on page 5 of the Bar's comments inaccurately portrays "Net 1977 Fees". The Client Security Fund fee is in addition to the general membership fees charged by the State Bar. Any reduction in the Client Security Fund fee has no effect on general membership fees. In addition, the State Bar is authorized to charge a \$10 annual Building Fund fee, which is not represented in the Bar's table.

DEVELOPING WORKLOAD STANDARDS AND PROJECTIONS FOR STATE BAR ACTIVITIES

Where applicable, quantified analysis provides perhaps the most objective evaluation of performance and future projection. Not all State Bar activities may be amenable to such an analysis. The following criteria may be used to determine the applicability of quantified workload analysis to each State Bar department:

- The extent to which workload is a function of a particular (or several) workload unit(s). The unit need not perfectly gauge all work nor must the resources necessary to process a work unit be uniform. What is important is that the unit reasonably reflect the bulk of resources generally applied to process the work.
- The history or convenience of collecting statistical trend data for the workload unit(s) and for the staff time or other resources spent processing the work.
- The simplicity of a formula which realistically relates average workload processed to average staff time and other processing expenses.

It is likely that some portion of activity in each department is not amenable to workload unit analysis. Expenses for such activities can be calculated in a separate "other" category. Projecting "other"

needs is a function of its own history or trends in the quantifiable workload.

Once workload units have been chosen, convenient ways should be developed to relate activity to expenses. Most State Bar expenses are salaries. Where appropriate, staff timesheets should be developed to provide data on staff time devoted to each workload unit. Disciplinary Enforcement has found that recording such hours requires only about five minutes of each attorney's day. Another approach is to statistically sample representative workload periods rather than keep time reported on a regular basis.

Where program expenses are not so significantly related to staff time, such as in the Print Shop, a different expense unit, such as total printing costs, may be appropriate. Travel costs are another example. Cost projections might be based on historical patterns of attendance and claims submissions for scheduled meetings.

Statistics should also be kept to show trends in the workload units. Some statistics are already available in many departments. For each type of workload, formulae relating workload and expenses can be developed by dividing the number of appropriate staff hours (or other costs) devoted to processing each unit by the number of units processed. The resulting average time (or cost) to process one unit may then be multiplied times projected workload trends to determine future requirements. In calculating staff needs, different averages should

be calculated for different staff levels (professional, paraprofessional, and clerical) except when one staff level's activity is a function of another's. For example, clerical tasks may be a function of attorney work in some departments.

We estimate that compiling monthly data and computing monthly workload standards for the entire State Bar should require less than half of a clerk's time.

AGENDA ITEM

FEBRUARY 6(a)(1)

Membership Fee Bill

Why An Increase In Fees Is Necessary in 1977

The budget for those expenses covered by the present fee structure for 1976 is	\$4,596,023
Projected Increase in Expenses for 1977	881,255
Deficit in 1976	<u>350,073</u>
Revenue Need in 1977	\$5,827,351

Based on the above, our present fee structure continued in 1977 would result in a deficit position in excess of \$1.3 million.

It is proposed that our fee structure be increased to the following which based on our projected active membership for 1977 would result in revenue available to cover 1977 expenses in addition to the 1976 deficit.

	<u>Projected Active Attorneys</u>	<u>Proposed Fee</u>	<u>Amount Of Increase</u>	<u>Revenue</u>
0 - 2 Years	\$ 11,000	\$ 60.00	\$ 10.00	\$ 660,000
2 - 5 Years	12,000	85.00	15.00	1,020,000
Over 5 Years	31,500	125.00	35.00	<u>3,937,500</u>
				\$5,617,500
		Other Income		<u>272,000</u>
		Total		<u><u>\$5,889,500</u></u>

The budget for calendar year 1976 as adopted by Board of Governors of the State Bar of California, may be capsulized as follows:

Revenue	\$ 5,913,950.00
Expense	6,215,726.00
Deficit	\$ (301,776.00)

This report, however, will concern itself only with those expense functions funded by the membership fees. Those functions having a separate revenue structure which support their expenditure are deducted as follows:

	<u>Revenue</u>	<u>Expense</u>
Budget as Adopted	\$5,913,950	\$6,215,726
Less -		
Bar Examiners	1,524,000	1,336,219
Legal Specialization	128,000	111,521
Taxation Section	16,000	15,963
Overhead Expenses charged to these Departments		156,000
	<u>\$4,245,950</u>	<u>\$4,596,023</u>

Our deficit in expenses covered by membership fees for calendar year 1976 \$350,073

1976 BUDGET AND PROJECTIONS FOR 1977
BY NATURAL EXPENSE CLASSIFICATIONS

	Adjusted 1976 <u>Total</u>	Projected 1977 <u>Total</u>
EMPLOYEE COSTS:		
Salaries (including O/S)	\$2,616,093	\$3,191,380
O/S Services - Personnel	29,965	29,965
Employee Benefits (P/R Taxes, Group Insurance, PERS, Recruiting Expense, Employee Parking Benefits)	433,462	530,462
TRAVEL:		
Board of Governors	43,000	51,600
Staff	64,732	77,332
Committees)		
Executive Committee)	237,892	285,470
Disciplinary Hearings)		
Entertainment	3,470	3,470
SUPPLIES & SERVICES:		
Materials & Supplies)		
Computer Services)	247,126	272,126
Printing)		
O/S Services - Other)		
Equipment - Rental & Repair	88,264	103,264
Rental - Office Space	37,920	48,000
Repairs & Maintenance - Building	48,684	60,684
Telephone	127,754	127,754
Utilities	32,089	42,089
Postage)		
Delivery Services)	105,549	115,549
Professional Fees	81,900	81,900
Reporting & Transcripts	164,000	190,240
Investigations)		
Witness Expense)	64,080	80,100
<i>Journal</i> - Printing	120,000	132,000
Newsletter)		
Law In Action)	92,166	92,166
Representation	7,500	7,500
Resolutions	25,000	30,000
Insurance	16,150	20,000
Library Upkeep	10,866	10,866
Elections	3,100	
Moot Court	1,500	
Achievement Award	500	
LIAFS	26,000	26,000
Miscellaneous	23,261	28,361
TOTALS	<u>\$4,752,023</u>	<u>\$5,633,278</u>

ANALYSIS OF 1977 INCREASES

Planned Manpower Increases 1977

<u>Department</u>	<u>Professional</u>	<u>Para- Professional</u>	<u>Clerical</u>	<u>Total</u>
Fiscal Affairs			2	2
Central Services		1	2	3
Print Shop			1	1
General Counsel	1		1	2
Discipline - Administration		1	2	3
Discipline - Enforcement	4	2	4	10
Investigators		3		3
Committee Assistance	1		2	3
Membership Records			1	1
Legal Services		1	1	2
Grant Programs		1	1	2
Unauthorized Practice of Law	1			1
	<u>7</u>	<u>9</u>	<u>17</u>	<u>33</u>

Salary Projections

7 Professionals at \$15,000/annum	\$105,000	
9 Para-Professionals at \$12,000/annum	108,000	
17 Clerical at \$9,000/annum	<u>153,000</u>	\$366,000

Planned 8% increase to employees of
record 12/31/76

209,287

Increase in Salary Expense

\$575,287

PERS Contribution for new employees and
salary increase at 10%

57,000

PERS Contribution increases at 1% of gross
salary at 12/31/76

26,000

Blue Cross increases in 1977

14,000

Increase in Employee Benefits

97,000

Conservative increases in other natural expense classifications
have been made based on:

1. Increases by suppliers which have been announced.
2. Increasing volume.
3. Needs of new facility forecast for completion in mid 1977.
4. Continued inflation.

JUNE 1976

INSIDE THIS ISSUE

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- More on Advertising
- Conference Call

THE STATE BAR OF CALIFORNIA

Reports:

THE FEE INCREASE: A STATEMENT

by

State Bar President David S. Casey and
President-Elect Ralph J. Gampell

Why a fee increase?

In short, the State Bar requires more money from its members because more services are being demanded of the State Bar:

★ As the Bar membership grows, increased departmental activity and higher administrative costs result, although not necessarily in direct proportion.

★ As more complaints are filed
(Continued on page 8)

Fee Increase

(Continued from page 1)

against attorneys, disciplinary costs increase.

★ As the Bar responds to legislative, judicial and consumer demands for increased public services, operating expenses inevitably rise.

By the end of 1976, the State Bar is projected to have a \$430,000 deficit. Following is a brief dollars-and-cents explanation of how we shall have arrived at that point.

HISTORY OF THE DEFICIT

In 1974, the Board of Governors asked the Legislature for authority to increase members' annual fees by amounts not to exceed \$45. This request was made to sustain ongoing and projected programs over the next several years. The Legislature granted only a \$10 increase to become effective January 1, 1976.

That decision, added to the state of the 1974-75 economy, and the Bar's efforts to meet growing membership, disciplinary and public service demands, resulted in a \$70,000 deficit at the end of 1975.

The Bar's 1976 financial picture was shown in February *Reports*: a total budget of \$6,215,721, with a deficit of \$301,776. (This took into account the self-sustaining Bar Examination program.) Later this year, unanticipated litigation became necessary in the Travelers Professional Liability suit, raising the 1976 deficit projection to \$360,000.

Hence, 1976's year-end total deficit of \$430,000.

FINANCIAL OUTLOOK '77

Because the Bar has no alternative but to keep pace as its membership grows and demands mount for even more effective discipline and other public services, 1977's expenses are expected to increase over this year's by approximately \$880,000. But it should be kept in mind that even if the requested fee increase does not go through and the 1976 level of expenditures is maintained, there will still be a 1977 deficit of \$350,000. (It is to be noted that this estimate is conservative: it assumes no increase of staff and does not take into consideration inflation.)

Altogether, adding up the 1975, 1976 and prospective 1977 deficits, plus increased 1977 expenses, it is evident that an increase in revenue of slightly more than \$1.6 million is

necessary. The one-year fee increase bill now before the Legislature would create that necessary revenue. In addition, that bill is designed to keep fees for the newest members of the Bar at a minimum:

Years Admitted	1976 Fee	Proposed 1977 Fee
0-2	\$50	\$ 55
2-5	70	85
5-10	90	115
10 and over	90	130

Our discussion so far has been couched only in terms of dollars-and-cents. We would like to turn now to the staff story behind the estimated 1977 expense increase.

WHAT'S IN AN INCREASE?

Of the increased 1977 costs, roughly 75% will be allocated to personnel as follows:

New personnel (33) ..	\$366,000
Merit increases to existing positions ..	209,000
Increase in cost of benefits (includes new positions)	97,000
	<u>\$672,000</u>

Why—and where—does the State Bar need 33 more people?

★ 16 of the 33 (four attorneys, six para-professionals including three investigators, and six support staff) will have to be added in the disciplinary area.

As you know, discipline is a function mandated by statute. The number of additional personnel requested was based not only upon generally accepted ABA standards regarding the ratio of staff required to adequately handle that mandated function but also upon State Bar statistics relating to workload.

That number has increased because the number of complaints and resulting disciplinary proceedings have increased 51% over the past five years—an average increase of 10% per year. Given the projected increase in the number of practicing attorneys in California (approximately 5,000 per year), the growing public awareness of the individual's ability to submit a complaint against an attorney, and legislation expanding the areas open to complaint and disciplinary proceedings, the Bar's future disciplinary workload can certainly be expected to increase at a rate exceeding that of the past five years.

★ Six of the 33 new personnel will work in the administration of the Bar (one para-professional and five support

staff members). This increase is necessary largely because of the Bar's growing membership: there were 4,600 new members in 1975, and 5,100 projected for this year.

★ The remaining 11 positions are sprinkled throughout the Bar's various departments. Increased departmental activity reflects both the increased membership and, primarily, rising legislative, judicial and consumer demands for Bar-sponsored public service activity. If the law is to remain a self-regulating profession, the Bar must respond fully and promptly to those demands.

COST-CUTTING

At this point, it should be noted that the Bar Board and staff have not merely sat back and watched costs spiral.

The Bar is changing from a labor-intensive operation to one geared to take advantage of computer technology. We believe this will mean a much smaller growth of personnel in the future, with resulting cost savings in the administration of the State Bar. Accounting and personnel systems have already been computerized wherever possible.

We have developed a Classification and Compensation Policy which allows for better manpower planning.

We are investigating our present system of membership records with an eye toward total computerization.

We have instituted new budget preparation systems which, in fact, enabled us to cut \$300,000 from the 1976 budget before its adoption.

IN SUMMARY

We requested the fee increase because we had no choice.

The price tag on State Bar operations had to go up given the swelling membership roles . . . the escalating number of complaints for the mandated disciplinary function . . . essential responses to stepped-up demands for public service, coming from all sides.

There is no way the State Bar can alter the facts of the situation.

We have, however, made strides in cost-effective management and realize there is more to be done.

The one promise we can make to you is that we will continue striving to meet the demands placed upon the State Bar in the most efficient ways possible—while representing you, the individual member, as effectively as possible on all fronts.

1976 BUDGET AND PROJECTIONS FOR 1977^①

	<u>1976</u> <u>Total</u>	<u>Projected</u> <u>1977</u> <u>Total</u>
EMPLOYEE COSTS:		
Salaries	\$2,616,093	\$3,191,380
Outside Services—Personnel	29,965	29,965
Employee Benefits		
Payroll Taxes, Group Insurance, PERS, etc.	433,462	530,462
TRAVEL:		
Board of Governors	43,000	51,600
Staff	64,732	77,332
Committees		
Executive Committee }	237,892	285,470
Disciplinary Hearings }		
SUPPLIES & SERVICES:		
Materials & Supplies		
Computer Services }	247,126	272,126
Printing }		
O/S Services—Other }		
Equipment—Rental & Repair	88,264	103,264
Rental—Office Space	37,920	48,000
Repairs & Maintenance—Building	48,684	50,584
Telephone	127,754	127,754
Utilities	32,089	42,089
Postage		
Delivery Services }	105,549	115,549
Professional Fees	81,900	81,900
Reporting & Transcripts Fees	164,000	190,240
Investigations		
Witness Expense }	64,080	80,100
Journal—Printing	120,000	132,000
Newsletter		
Law In Action }	92,166	92,166
Representation	7,500	7,500
Resolutions	25,000	30,000
Insurance	16,150	20,000
Library Upkeep	10,866	10,866
Law In A Free Society	26,000	26,000
Miscellaneous	31,831	31,831
TOTALS	<u>\$4,752,023</u>	<u>\$5,638,278</u>

① Listed expenses are only those covered by the membership fee. The expenses of the Bar Examiners, Legal Specialization and Sections which are self-sufficient do not appear above.

Auditor General's Statement of
Underlying Assumptions and Cautions Relating to
Cash Forecasts

Introduction

Assumptions used for purposes of cash projections represent estimates of future events and are subject to uncertainty as to possible changes in economic, legislative, and other circumstances. As a result, the identification and interpretation of data and their use in developing and selecting assumptions, from among reasonable alternatives, require the exercise of judgment. In our judgment, based on our study, the assumptions used for purposes of the projections are reasonable and appropriate and the projected outcome is therefore reasonable. To the extent that the assumed events do not materialize, the outcome may vary substantially from that projected.

Major Cash Forecast Assumptions

1. The State Bar's timing for the receipt of revenue and disbursements for expenses will not vary significantly from historic trends with the exception of assumption (2) below.
2. The Bar will deposit receipts in a timely manner.
3. Bar membership will rise according to projections based on data provided by the Bar.
4. Advance receipt of membership and Bar Examination fees will continue with approximately the same timing as prior years.

5. The Bar's expenses will be disbursed as the Bar has proposed.
6. The Bar will be able to temporarily borrow to meet a projected cash deficiency in November 1977.

Office of the Auditor General

cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
Secretary of State
State Controller
State Treasurer
Legislative Analyst
Director of Finance
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
California State Department Heads
Capitol Press Corps