

COMMITTEE OF BAR EXAMINERS OPEN SESSION AGENDA ITEM

AGENDA ITEM: April 2016 – O-300
DATE: April 27, 2016
TO: Subcommittee on Operations and Management
FROM: Gayle Murphy, Senior Director, Admissions
SUBJECT: Future Admissions Budgets and Fees

BACKGROUND

During the Committee of Bar Examiners' (Committee) March meeting, it considered a report concerning the State Bar of California's new reserve and indirect costs policies.

With regard to indirect costs, the following allocations have been made based on "actual direct costs as % of total State Bar direct costs":

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Board of Trustees Election	\$ 49,360	\$ 48,405	\$ 40,581
Appointments	\$ 20,891	\$ 548	\$ 1,571
Executive Director's Office	\$460,739	\$ 74,928	\$110,543
Finance	\$650,475	\$791,697	\$664,716

The allocations noted above are based on percentages of costs, rather than FTEs or square footage as other categories of costs are allocated, such as Human Resources, General Counsel, General Services, IT, etc.

With regard to the Reserve Policy, according to a Board of Trustees' agenda item, there is \$3,884,000 in the Admissions Fund's reserve, which is 19.26% of the total operating budget. A minimum reserve would be \$3,428,220 and a maximum would be \$6,049,800.

According to the latest figures available, the status of the Admissions Fund is as follows:

2016 Budget:

Revenue	\$20,256,168
Expenses	\$22,267,365
Carry Forward	\$3,884,000
Indirect Costs	\$5,155,200

DISCUSSION

In order to build budgets for the future, a good starting point is to attempt to predict the number of possible examination takers. This becomes a bit difficult, however, as the number of applicants who are successful/unsuccessful can vary from one administration of the examination to the next and the numbers graduating from law schools (in and out-of-state), as well as attorneys from other states electing to take the examination, will also vary according to factors that may not be known at the time.

Greg Shin, Director for Operations and Management, has prepared a summary of California law school enrollment data and other indicators that show that, while there has been much in the news about declining law school enrollment, the decline has not significantly impacted the number of applicants taking the California Bar Examination. The numbers are down, but only by about 2%. Part of this is due to the lower passing rates, which has caused the number of repeaters to climb past predictions used to prepare past budgets. The summaries he has prepared will be distributed at the meeting. According to an article in the National Law Journal: “Early indicators point to an increase in the number of people applying to law school, following a five-year decline.” Also a factor to be considered is the lower LSAT scores of many of the applicants being admitted to law school, which suggests that the number of passing applicants may not increase over the next couple of years. Lower passing rates, generally, have resulted in an increase the number of repeaters taking the next administration of the examination.

These factors seem to support using the numbers of applicants experienced in 2015 as a base for preparing future budgets. The 2016 budget was prepared using a slightly lower number of applicants applying. It appears, however, that the number of applicants actually applying was higher than originally projected. Because of that experience, and due to fee increases that went into effect with the February 2016 examination, revenue is higher than expected for the February 2016 administration of the examination. A short summary of the 2016 budget/actuals for the two 2016 bar examinations (July revenue will continue until June), compared to 2015, follows:

	<u>Applicants Taking</u>	<u>Revenue Budgeted</u>	<u>Actual</u>
February 2015	5230	\$4,155,187	\$4,260,789
July 2015	8736	\$6,546,539	\$6,564,208
February 2016	5010	\$4,476,792	\$4,999,196*
July 2016	6020**	\$6,897,996	N/A

* As of 2/16 Operating Statement; refunds not yet processed.

** Year to date; last year at this time 6699

The increase in revenue in 2016 over what was budgeted is in large part due to the lower passing rate from the July 2015 California Bar Examination, which was 46.1% (the lowest in almost 30 years) and unexpected. Using the above as a guide, it appears, at a minimum, that the 2016 budget is currently approximately \$500,000 over budget in revenue alone.

As discussed in previous meetings, revenue and expenses in the Admissions Fund cover many other functions, such as law school regulation, MCLE Provider Certification, the Multijurisdictional Practice (MJP) program, and special admissions (which includes Pro Hac Vice, Out of State Attorney Arbitration Counsel (OSAAC), and the Practical Training of Law Students (PTLS) Program).

According to the 2015 final Operating Statement:

	<u>Budget</u>	<u>Actual</u>
Total Admissions Revenue	\$20,256,168	\$20,428,733
MJP Revenue:	\$123,860	\$172,777
MCLE Provider Revenue:	\$237,000	\$256,486
Law School Regulation:	\$105,000	\$125,087
PTLS	\$120,740	\$114,840
Pro Hac Vice	\$125,000	\$122,750
OSAAC	\$ 32,000	\$ 29,250

With regard to the expenses associated with the programs above: (1) the MJP costs are integrated into the LA Operations Overhead cost center; (2) the MCLE Provider 2015 cost center actual expense was \$286,855; (3) the expenses for Law School Regulation were \$447,125; and (4) PTLS, Pro Hac Vice and OSAAC are combined into a special admissions cost center, which total revenue in 2015 was \$266,840, compared to the expense in 2015, which was \$311,031. In 2015, the indirect costs allocations were distributed between the cost centers, which made it easier to determine the total cost of the programs – except for the Admissions management costs, which have not been accounted for in the expense associated with administering each of the programs. In order to recognize that expense as part of the cost of administering these programs, an appropriate method to use might be to take a percentage of total actual costs of the Admissions overhead cost center, based on each cost center’s percentage of the total Admissions cost, and add that to each function that has a cost center. The 2015 actual expense for the Admissions overhead cost center was \$832,624. Using this methodology, the following are the costs of administering the following programs:

Law School Regulation:	$\$447,125 + \$16,652$ (2% of ADM Overhead) = \$463,777
MCLE Provider:	$\$286,855 + \$8,326$ (1% of ADM Overhead) = \$295,181
Special Admissions:	$\$311,031 + \$12,489$ (1.5% of ADM Overhead) = \$323,520

Using this analysis and 2015 figures, it appears that the fees charged for the law school regulation function are underfunding the program by \$338,690 (73%), the fees for the MCLE providers do not cover the program costs by \$38,695 (13%), and the special admissions fees revenue of \$266,840 does not cover the costs associated with administering the programs by \$56,680 (18%). It would be appropriate to recommend that fees be adjusted to cover those costs, although the increase to the fees charged for law school regulation may be so significant that it would be difficult to achieve. Two of the three programs under Special Admissions have fees set by statute, which also might be difficult to change. Since the fees haven’t been adjusted for some time, proposed adjustments to the MCLE Provider fees should encounter fewer roadblocks.

Before specific adjustments are recommended, however, the increased indirect costs allocations that were added to the 2016 budget need to be taken into account.

Using the 2016 budget as a base, if the fees are raised to cover the costs discussed above, and after subtracting the costs of administering the separate programs from the general admission fund (using the cost figures from 2015 as noted above), we are left with \$19,173,660 in revenue and \$21,184,857 in expenses, which would indicate that revenue is not covering the costs of running the Admissions programs. In past years, however, the carry forward has been used to make up the difference until another fee adjustment to bring things into balance has been approved. With the new reserve policy, this approach may no longer be viable.

Before assuming a fee adjustment is necessary, another variable to consider is the impact of the modified California Bar Examination. At the time the Committee approved the two-day examination, it was thought there would be a savings of approximately \$1,100,000 associated with administering and grading of the examination. In 2017, the February examination will be administered over three days; in July 2017, the examination will be administered over two days. The projected savings could be divided in two, which means that in 2017, we would expect to see approximately \$500,000 in savings (although since it is the larger examination, it may be slightly higher).

If the 2016 budget were used for 2017, the anticipated income would remain the same, but the costs would drop to \$20,684,857, which would mean that projected costs still would exceed projected revenue by approximately \$1,500,000. In 2018, again if revenue stays the same, but costs are reduced by \$1,000,000 due to the modified examination, there would only be approximately \$500,000 not covered.

Another factor to be considered, too, is the cost associated with implementing a new Admissions data processing system, for which an RFP is expected to be released shortly. It is difficult to predict how much such a system might cost, but it could be in the neighborhood of 2-3 million dollars. A million dollars has been set aside in the IT cost center for this purpose, but the acquisition of additional funds to cover the cost of the new system may be necessary.

The figures used in this agenda item, while real, are being used primarily to facilitate a discussion on these issues and should only be used in that context. Depending on the outcome of the Committee's discussion, the State Bar's Office of Finance may be asked to assist in preparing final numbers for determining percentages of overhead that should be used, etc. Bottom line, the Committee should consider: 1) whether the carry forward (now the "reserve") should (or can) be used to cover the difference in revenue vs. expenses in the coming years; 2) whether there should be a discussion with the Board of Trustees concerning the increase in the indirect costs allocations; 3) whether the "special" programs should be self-sustaining; and 4) whether certain adjustments to the fees charged for services the Office of Admissions provides should be sought.

Before any recommendation can be prepared regarding future budget planning and the appropriate fees that should be charged, it would be helpful to have guidance from the Subcommittee regarding the issues identified above. In any event, it appears that if fee adjustments are necessary, the soonest that would be necessary and could be

implemented would be in connection with administration of the July 2017 California Bar Examination, for which applications will be made available March 1, 2017.

RECOMMENDATION

Pending