



WHITE PAPER

# A LAWYER'S 7-POINT PLAN FOR TRUST ACCOUNT MANAGEMENT:

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# Introduction

Many jurisdictions require attorneys to maintain lawyer's trust accounts, and those accounts, and jurisdictional rules, come in many shapes and sizes. As a lawyer, it's your job to act as a fiduciary or virtual "trustee" of client funds, and as such, you must scrupulously follow stringent standards of good faith and transparency. While most of us associate this fiduciary obligation only with money, your duty extends to the protection of ANY client property.

Though there may be some debate about the exact event that led to the creation of trust accounts, the purpose is clear: to safeguard and protect client funds, while also protecting the lawyer from the perception of improper, or illegal behavior. In order to avoid any appearance of impropriety, lawyers are typically required by state, provincial or bar rules to segregate client funds from business funds.

Considering the potential for confusion about all the regulations governing trust accounts – and the extremely serious consequences for violating them – it's worth taking the time to refresh your memory to make sure your firm stays lock-step in line with every requirement.



# 1. Avoiding the appearance of impropriety: Keeping trust funds separated from firm funds

A lawyer trust account is essentially a business checking account or its equivalent, established by the firm to hold client funds. FUNDS DEPOSITED INTO A TRUST ACCOUNT ARE NEITHER YOUR PROPERTY, NOR YOUR FIRM'S.

Depending on the jurisdiction, a law firm must adhere to one of two standards:

1. Maintain a single account to hold all client funds or property, with the lawyer responsible for keeping up with fund ownership.
2. Keep individual trust bank accounts so that one client's funds are not commingled with another's.

No matter which scenario is mandated, it's only under the very rarest of circumstances that client funds may be commingled with a lawyer's business funds. In the vast majority of cases, client funds must be deposited into a separate attorneys' trust checking account and designated as such. Trust account funds may not be utilized by the law firm until they are earned. This further ensures accurate record-keeping, as well as the integrity of the firm.

*Funds deposited into a trust account are neither your property, nor your firm's.*



## 2. Watching over the institutions watching over your clients' trust funds

Many states and provinces require that lawyer's trust accounts be maintained in approved financial institutions within the borders of the state or province where the lawyer's office is located. For example, the rules regulating the Georgia Bar are very clear about banking institution type and location:

Required Bank Accounts: Every lawyer who practices law in Georgia, and who receives money or other property on behalf of a client or in any other fiduciary capacity shall maintain, in an approved financial institution as defined by this Rule, a trust account or accounts, separate from any business and personal accounts. Funds received by the lawyer on behalf of a client or in any other fiduciary capacity shall be deposited into this account. The financial institution shall be in Georgia or in the state where the lawyer's office is located, or elsewhere with the written consent and at the written request of the client or third person.

Other states have very similar requirements. Note specifically that Georgia requires that a

lawyer maintain an account in "an approved financial institution."

Comment one on the same reference states: "Each financial institution wishing to be approved as a depository of client trust funds must file an overdraft notification agreement with the State Disciplinary Board of the State Bar of Georgia. The State Bar of Georgia will publish a list of approved institutions at least annually."

Similarly, the Law Society of Manitoba requires that a Manitoba lawyer's trust account must be opened within the borders of the province at a chartered bank, at a trust company authorized by law and insured by the Canada Deposit Insurance Corporation, or at a properly incorporated credit union . Thus, it is inherent in the rules that you know WHERE you may open and maintain an attorneys' trust account.





### 3. Knowing the rules for fees earned in advance: When in doubt, go with the trust account

Fees earned in advance can create a very slippery slope for law firms. When in doubt, put client retainer funds into your properly maintained attorney trust account.

In limited circumstances, some jurisdictions may permit a law firm to deposit monies paid by a client in advance into the firm's operating account. For example, the New York Rules of Professional Conduct do not mandate what a lawyer should do with retainer funds paid in advance of legal fees, although there are ethical opinions providing guidance.

N.Y. State Bar Opinion 570 (1985) noted that the drafters of the Code of Professional Responsibility did not consider advance payments of fees to be client funds necessitating their deposit in a trust account. The opinion observed that:

Normally, when one pays in advance for services to be rendered or property to be delivered, ownership of the funds passes upon payment, absent an express agreement that the payment be held in trust or escrow, and notwithstanding the payee's obligation to perform or to refund the payment. The lawyers who drafted the Code should not lightly be assumed to have overlooked these fundamental principles in choosing the language of DR 9-102(A) .

New Jersey takes a similar position: Absent a clear understanding that the retainer fee be separately maintained, the funds need not be deposited in an attorney's trust account . Compare New York's and New Jersey's position with that of the Florida Bar, which clearly states that:

Earned fees, including 'true retainers', must not be placed in the trust account. Unearned fees and advances for costs must be placed in the trust account. Nonrefundable fees are permissible, but remain subject to the rule regarding clearly

excessive fees. When charging a flat fee (a portion of which will be used to pay costs), the lawyer must deposit into the trust account any unearned fee, as well as the estimated amount of costs. An attorney who charges a flat fee, a portion of which will be used to pay costs, must deposit into the trust account any unearned fee, as well as the estimated amount of costs.

Further, the 2010 amendment to this rule requires that nonrefundable fees be confirmed in writing.

Bottom line, be absolutely certain that the account into which you place retainers, fees in advance, flat fees and non-refundable fees is permitted in your state, and do so with caution. If there is ANY doubt, place the funds in your attorney trust account.

## 4. Where the interest goes: Understanding Interest on Lawyer Trust Accounts (IOLTA) regulations

The Interest on Lawyer Trust Accounts (IOLTA) program was first established in Canada and Australia in the late 1960s and early '70s as a method to generate funds for indigent legal clients. In the late '70s, the Florida Bar established the first U.S. IOLTA program. In 1981, after the Florida legislature permitted the establishment of interest-bearing checking accounts and the IRS gave its blessing, the Florida Bar Foundation launched the first IOLTA program. California, Maryland and Idaho soon followed.

Today, all 50 states, the District of Columbia and the U.S. Virgin Islands operate IOLTA programs. Forty-four states require lawyers to participate in IOLTA. Lawyers can opt out of participation in 4 jurisdictions (Alaska, Kansas, Nebraska, Virginia), and participation is voluntary in two others (South Dakota and the Virgin Islands) .

So, what does it mean if you are in a state with a mandatory IOLTA program? IOLTA.org explains as follows:



A lawyer who receives funds that belong to a client must place those funds in a trust account separate from the lawyer's own money. Client funds are deposited in an IOLTA account when the funds cannot otherwise earn enough income for the client to be more than the cost of securing that income. The client - and not the IOLTA program - receives the interest if the funds are large enough or will be held for a long enough period of time to generate net interest that is sufficient to allocate directly to the client.

Every state, along with the District of Columbia and the Virgin Islands, operates an IOLTA program. In 2009, the U.S. IOLTA programs generated more than \$124.7 million nationwide. These funds, together with state and federal appropriations as well as private grants and donations, enable nonprofit legal aid providers to help low-income people with civil legal matters such as landlord/tenant issues, child custody disputes and advocacy for those with disabilities.

## 5. What you don't know CAN hurt you: Covering your back with legal-specific accounting software

Considering the options available to law firms today, it can be foolhardy to even think about maintaining an attorney trust account without legal-specific accounting software. Accounting software made for law firms includes three-point trust account reconciliation you can't get from generic accounting software without jumping through hoops. Maintaining trust accounting in generic business accounting programs is flirting with disaster if your firm is audited, or if one of your clients complains to the bar association.

Before you commit to any accounting software, make sure that it allows for:

- 1. Three-Point Trust Account Reconciliation**
  - Simply put, your trust account must



be maintained in such a way that you can, at any time, decipher three points of financial data in a very balanced way.

- a. **Point one:** What is the balance in the trust bank?
- b. **Point two:** What is the balance in your trust liability account on your balance sheet? Does point two match point one at all times and for all dates?
- c. **Point three:** Can you break down the balance in the trust bank on a client-by-client basis?

- 2. **Client Trust Ledgers** – You must be able to track all transactions related to your client from the initial deposit to trust through the last disbursement from trust. Your software should be able to do this filtered by client, matter, date range and transaction type.
- 3. **Easy movement of trust funds** – You should be able to easily move trust funds to your operating account in payment of an outstanding invoice and/or to reimburse your firm for disbursement work in progress (WIP). In some jurisdictions, it is permissible to transfer funds from trust to operating accounts immediately before billing so that the transaction can be reflected on your client/matter invoice.
- 4. **Easy production of trust reports** – Nothing would be worse than to have to scramble to provide simple, basic trust account reports when you have a state

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bar trust account auditor standing in front of you demanding them. But more importantly, it is important to always know your trust balances on a matter by matter basis and ensure that the total balance (matter by matter) equals the balance in your IOLTA or trust bank account for the same date range.

In addition, you must be 100% sure that the funds deposited on behalf of your client have actually been cleared by the bank BEFORE disbursement. If funds are disbursed before the check clears, you have effectively allocated trust funds that didn't belong to the client, and this violates most bar and law society regulations.

What's more, it is very important to recognize that "available" funds are not the same as "cleared" (100% collected) funds. When a check or other transaction is made to a financial institution, it may take the bank several days before the full amount of the deposit is collected and you may ONLY disburse funds from trust accounts that have been collected.

## 6. Banking fees:

Make sure you know the rules even when your banking institution doesn't

Interestingly, many banking institutions that qualify as "approved" by their respective states and provinces don't actually understand the nuances of an attorney trust account. For example, under rare circumstances (and Wisconsin is one of the rare states permitting this), attorneys are allowed to commingle firm funds and client funds in trust, while most states and provinces PROHIBIT such allowances no matter the circumstances.

The onus is on you, the attorney, to ensure that his or her bank adheres to the rules of the state or provincial bar association. This includes prohibiting banking fees, check printing fees or even credit card merchant account fees on an attorney's trust account. Because the attorney's trust account holds funds that DO NOT belong to him or her, a bank drafting the account to cover such



fees and charges violates the rules regulating attorney's trust accounts.

**ATTORNEY BEWARE:** Banks that are approved by the state bar may still unwittingly violate the rules governing banking trust account regulation. Ultimately, **YOU ARE RESPONSIBLE FOR MAKING SURE THAT TRUST ACCOUNT RULES ARE FOLLOWED TO THE LETTER.** If necessary, spend the time to educate your banking institution. Direct that any fees on trust accounts should instead be drafted from the firm's operating account. That includes bank charges, overdraft fees, check or deposit slip fees, printing fees and credit card merchant account fees. (And yes, you may find that the credit card merchant requires your direction as well.)

## 7. The lawyer discipline system: Understanding the consequences of not understanding every rule

Lawyers who fail to strictly adhere to the rules regulating the maintenance of lawyer's trust accounts are likely to become part of the lawyer discipline system administered by their state bar association. Lawyers may face severe sanctions, including disbarment.

Trust account rules and regulations are in place to protect the public from lawyer misconduct. It's imperative that lawyers have the information they need to adhere to the disciplinary rules and protect themselves from the grievance process. Every state and province maintains internal procedures to audit attorney trust accounts, oftentimes unannounced.

One example is the Law Society of Alberta's new Trust Safety program, which was implemented in January of 2011. The new regulations address concerns about rising threats to the security of trust funds by lawyers. Alberta employs certain control techniques that may require a lawyer to transmit his or her trust account records to the law society to demonstrate compliance. Similarly, the State Bar of California issues a handbook on client trust accounting that is over 100 pages long. Attorneys in California must be aware of and adhere to the rules. For example, maintaining personal funds in a California Attorney Trust Account as a cushion against overdrafts is NOT allowed and will expose an attorney to disciplinary measures. (However, maintaining a small "firm" balance in trust, is permitted in many jurisdictions.)

# PCLaw®

## From PCLaw | Time Matters™:

Making it easy to make trust manageable

One of the best things about legal-specific software such as PCLaw from PCLaw | Time Matters™ is that it is a program built to provide easy-to-manage-and-maintain attorney trust accounting that can save your firm from sanctions down the road. PCLaw provides robust trust accounting functionality, including three-point reconciliation, easy-to-read and understand client trust ledgers, simple trust transfer functionality (including functionality that will prevent anyone in your office from overdrawing a client's trust funds), as well as myriad reports that will satisfy even the most persnickety trust account auditor.

PCLaw includes this functionality and much more, yet there are still lawyers out there who don't use client-specific accounting software. For example, QuickBooks® – a wonderful business accounting program from Intuit, Inc. – does not include any features that help your firm comply with trust account rules by default.

QuickBooks users are often guided to the program because it's what their accountants and/or CPA's request. Unfortunately, those accountants are not always educated in the nuances of trust accounting and its requirements. Programs like PCLaw typically does EVERYTHING that QuickBooks can do, AND it automatically keeps you in compliance with trust account regulations.



# Conclusion

While some of these topics may on the surface seem frightening, all that's really required to stay in compliance with trust accounting rules is a healthy respect for those rules, along with legal-specific accounting software from a reputable company. With programs such as PCLaw working for you, there's no need for stress concerning trust account regulations.

PCLaw | Time Matters™ has you covered.

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Steven J. Best is an attorney as well as a certified law office software consultant. He is the managing partner of Affinity Consulting Group's Atlanta office. With an educational background in law, accounting and economics, Steve consults with law firms throughout the United States on legal office software, as well as sophisticated practice management solutions.

Best is a graduate of Rutgers University and Emory University School of Law. He is a member of the Florida and Georgia Bars and is also a certified consultant/trainer, maintaining certifications in several of the top practice management, time/billing/accounting, document management and document assembly applications, including PCLaw® and Time Matters®. Steve also consults with law firms on workflow management, financial management, trust account management and migrating to a paperless office environment. Steve is also a frequent lecturer at a variety of CLE and technology programs on topics surrounding legal technology, practice management, cloud solutions and document management/workflow. He co-chairs the annual Georgia ICLE program on legal technology. Steve has twice served on the LexisNexis Consultant Advisory Panel and is currently serving on the PCLaw Product Development advisory committee. He is a member of the ABA TechShow planning board for 2013-2015.

## Key trust account functions included with PCLaw®

The State Bar of Wisconsin, like the majority of states and provinces, requires that attorneys maintain trust account records for at least 6 years, including a chronological tracking of all deposits and disbursements (transaction register); individual client ledgers, including a chronological record of deposits and disbursements on a matter-by-matter basis; and a ledger of any fees and charges on the trust account. Additionally, Wisconsin (like its neighboring states) requires maintaining reports such as monthly bank statements, along with reconciliation and deposit slip reports. Further, Wisconsin mandates that the CLIENT/MATTER and REASON for the disbursement be noted in the memo field on the face of every trust check disbursed.

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