

# Trust Accounting Rules !

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# Topics to Be Covered

1. Trust Account Rules
2. Key Concepts
3. Trust Account Basics
4. Funds Go In (Deposit)
5. Funds Go Out (Disbursement)
6. Recordkeeping

# Topics to Be Covered contd.

7. Reconciliation
8. Safeguarding Funds from Embezzlement
9. IOLTA
10. FDIC Insurance
11. Random Audit Program

Must.

Always.

Never.



# Trust Account and IOLTA Rules

- NC Rules of Professional Conduct

- Rule 1.15, Preserving the Property of Others

- Rule 1.15-1, Definitions
    - Rule 1.15-2, General Rules
    - Rule 1.15-3, Records and Accountings

# 7 Key Concepts of Client Trust Accounting

# Key Concepts

## 1. Separate Clients Are Separate Accounts

- You are **NEVER** allowed to use one client's money to pay either another client's or your own obligations
- Keep a client ledger of each client's funds
- 10 clients in a trust account means 10 ledgers

# Key Concepts

## 2. You Can't Spend What You Don't Have

- Each client has only his or her funds available to cover their expenses.

Client A	\$1,000
Client B	\$2,000
Client C	\$3,000
<u>Client D</u>	<u>\$500</u>
Total	\$5,000

A check to Client D for \$1,500 will be paid for by Clients A,B and C. This is misappropriation of funds.

# Key Concepts

## 3. There's no Such Thing as a Negative Balance

In client trust accounting, there are only 3 possibilities:

- You have a **Positive** balance
- You have a **Zero** balance
- You have a problem. (**Negative** balance)

# Key Concepts

## 4. Timing is Everything

- Bouncing Checks vs. Advancing Funds = Equally deplorable
- Know your bank
  - When funds are available
  - Deposit deadline
- Don't help one client at the expense of another

# Key Concepts

## 5. You Can't Play the Game Unless you Know the Score

- “Running Balance” of the client
- “Running Balance” of the client trust account

# Key Concepts

## 6. The Final Score is **ALWAYS** Zero

- What comes in = What goes out
  - No more, no less
- Take care of small, inactive balances as soon as possible



# Key Concepts

## 7. **Always** Maintain an Audit Trail

- Be Descriptive
- **NEVER** make out a client trust account check to cash

# Trust Account Basics

- What is a trust account?
- Who **must** have a trust account?
- How many trust accounts does a lawyer need?
- Does each lawyer in a firm need a separate trust account?
- Is a lawyer ever required to establish a trust account for one client, or one transaction?

# Basics: Opening a Trust Account

- What bank should I use?
- How should I label my Trust Account?
- What type of checks **must** I use?
- Who may be a signatory?

# Basics: Trust Account Management

- May I delegate management to one lawyer in the firm?
- May I delegate management to a staff member who is not a lawyer?
- May I “link” my trust account with my business account?

# Basics: Abandoned or Unclaimed Funds

- What should I do with unidentified funds in my trust account?
- How do I escheat funds?

# Basics: Closing a Trust Account

- How do I close an account that has remaining funds?
- What if my law firm is under dissolution?

Funds Go In (Deposit)

# What Goes Into a Trust Account?

- Every receipt of money from a client or for a client which will be used or delivered on the client's behalf should be placed in the trust account or a fiduciary account.



# Funds Go In

- What about non-cash items?
- What about small sums of money?

# What Does Not Go in the Trust Account?

- No funds belonging to the lawyer may be deposited in the trust account except such funds as are necessary to open or maintain the account, or pay service charges, or are funds belonging in part to a client and in part presently or potentially to the lawyer.

# Funds Go In

- Should retainers be deposited in the trust account?
- What about funds belonging to an organization?

# Funds Go In: Depositing Funds

## 1. Depositing a mix of Trust and Non-Trust Funds

### Example:

Attorney fee	\$150.00
Recording fee	\$30.00
Sheriff fee	\$4.00
Total	\$184.00

What happens when: 1) Client writes check for \$184.00, 2) Client pays with 2 checks, 3) Client pays in cash?

# Funds Go In: Deposits

- Credit Card Payments From Clients

Funds Go Out

# Funds Go Out: Appropriate Disbursements

- May I use funds to pay legal fees or the claims of creditors?
- What if I have an interest in settlement or judgment funds received?
- May I disburse funds as an escrow agent in a manner not contemplated by the agreement?

# Appropriate Disbursements

- Conditional Delivery to a real estate agent
- Disbursing against provisionally credited funds
  - Good Funds Settlement Act



# Funds Go Out: Problems

- What if a Trust Account Check Bounces?
- Overdraws

# Recordkeeping

# Recordkeeping

- What Records are Required?
  - Record of receipts
  - All wire instructions
  - All bank statements
  - General ledger
  - Client ledger
  - Records of monthly and quarterly reconciliations
  - Any other records required by law

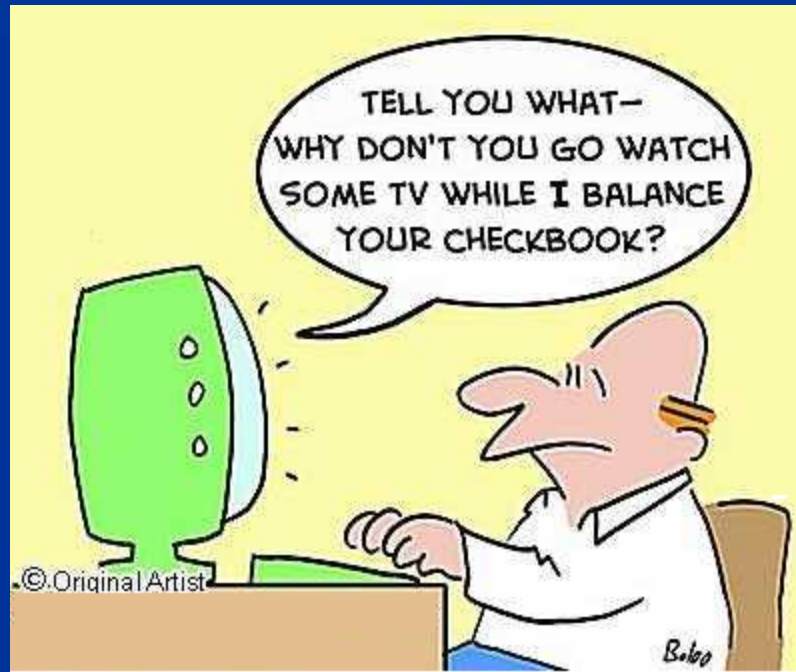
# Recordkeeping

- How long should I keep records?
- May I keep records electronically?
- How often **must** I provide an accounting to my client?

# Recordkeeping

- Manual Records vs. Electronic
  - Document deposits to and disbursements from
  - Maintain a current balance
  - Provide a means for reconciling monthly and quarterly
  - Retain records
  - Provide annual accountings

# Record Keeping Software



Fully integrated, legal-specific, trust  
accounting, time & billing, general ledger  
accounting software.

**(PCLaw, Abacus Accounting, Amicus  
Accounting, Juris)**

Legal-specific trust accounting software  
**(TABS3 Trust Accounts by STI, EasyTrust,  
SoftPro-Pro Trust (NC))**

Time & billing software with add-on  
integrated trust accounting,  
used by law firms  
**(TimeSlips, Time Matters)**

Non-legal specific, small business, accounting software  
**(QuickBooks Pro/Premier)**

Low-cost personal and home business financial software  
**(Quicken)**

“Make the most of what you already paid for.”  
**(Excel or Quattro Pro)**

**Non-automated trust account maintenance**

# Software Mistakes

- Over reliance on software
- Using the software wrong
- Creating the wrong reports



# Reconciliation

- What is reconciliation?
- Monthly Reconciliation
- Quarterly Reconciliation

# Quarterly Reconciliation Example

# 1. Reconciling General Ledger with Client Ledger

- Step 1: Write in clients names and client ledger balances in appropriate spots.
- Step 2: Add up client ledger balances, write in total in appropriate spot.
- Step 3: Compare “Total of Client Ledger Balances” with “General ledger balance”
- If no mistake found, move on.....

## 2. Reconcile the General Ledger with the Bank Statement

- Step 4: Fill in “Ending Balance per bank statement” with running balance as of last day covered by bank statement
- Step 5: Enter deposits made to the account, yet not captured on the Bank Statement
- Step 6: Enter total outstanding checks
- Step 7: Make sure that bank charges and interest credits are reflected in your records

# Likely Mistakes

- 1. Find a deposit or withdrawal on the bank statement that isn't in your ledger or checkbook register
- 2. An entry in the bank statement is different from the corresponding entry in the ledger

# Calculate Adjusted Balance

## ■ Step 8:

- Ending Bank Statement Balance
- PLUS All outstanding Deposits
- MINUS All outstanding checks
- PLUS Interest (if not directly to IOLTA)
- MINUS Bank Fees and Charges
- = Adjusted Balance

# Final Comparison

- The total of all client ledgers, general ledger, and adjusted bank balance should all match.
  - If yes, you are done. Save all records.
  - If no, go back and find error, or call bookkeeper.

# Safeguarding Funds From Embezzlement



# Practice Tips

- Do not act in haste
- Use Pre-numbered checks
- Cash is difficult
- Be wary of sole control of trust account activities
- Resolve discrepancies quickly
- Do not sign blank checks
- Keep documentation and review everything periodically
- Question lifestyle changes of individuals with access to trust account
- Examine signatures on trust account checks for forgery

# Practice Tips

- Check periodically with post office about mail pick up
- Reconcile trust account promptly after receiving bank statement
- Question a negative attitude or poor work performance of an employee maintaining the trust account
- DEVELOP AN OFFICE POLICY

# IOLTA

- What is IOLTA?
- How does it work?
- Which accounts must be IOLTA accounts?
- Does using an IOLTA account harm my client financially?
- What about out of state law firms?

# FDIC Insurance

- What is my responsibility when choosing a depository bank?
- Does FDIC insurance protect my trust account?
- How must I explain this to my client?

# Random Audit Program

- Authority
- Selection Process
- Scope of Audit
- Exemption from Audit
- Confidentiality
- Discipline
- Trust Accounting Compliance Program (TAC Program)

# Conclusion

- Remember the M.A.N....

... in order to please **The Man,**



NORTH CAROLINA  
STATE BAR

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...and hope to avoid **THE MAN!**





# True/False Quiz

1. Trust Account violations are governed by the “no harm, no foul rule.” A lawyer cannot be disciplined if the clients eventually get their money.

**FALSE**

# True/False Quiz

2. An intervening third-party criminal act, such as a book-keeper embezzling funds, relieves the lawyer of disciplinary responsibility.

**FALSE**

3. A check certified by a bank (a certified check) is normally as good as cash.

**TRUE\***

4. A lawyer may ethically protect against bounced checks and checks presented against insufficient funds by keeping a portion of lawyer's own money in the trust account as "float".

**FALSE**

5. A lawyer will not be subject to discipline for failing to reconcile the client trust account if no client funds have been harmed.

**FALSE**

6. It is permissible for the lawyer's fees to remain in the trust account after they are earned as long as the clients timely get their money.

**FALSE**