

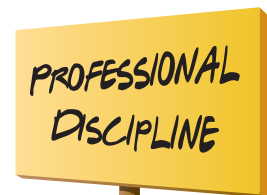
The Top Five Misuses of an IOLTA: The Road to Professional Discipline

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There is no quicker road to attorney discipline than the mishandling or misuse of a clients' funds account. Regardless of how an attorney may elect to handle her own finances, there are strict regulations concerning the handling of client and third-party funds. This is not an area where a lawyer can "just do it." Rather, the lawyer must be knowledgeable and strictly comply with the rules governing IOLTAs.

Here are the top five IOLTA abuses based upon a review of grievance decisions and cases over the past several years.¹ This is a list of "Don't's."

1. Do Not Commingle Personal Funds with Clients' Funds

Do not commingle the IOLTA funds with the law firm's or lawyer's own funds. The law practice should have two separate accounts: a law firm operating account and a clients' funds account. The lawyer must not keep personal funds in the IOLTA, with one small exception. There are a few basic rules.

First, Connecticut lawyers who hold clients' funds must hold the monies in an IOLTA.² This includes any advance payment for legal services,³ funds used in transactional work, or monies received from settlement proceeds. A lawyer who accepts retainers, in the absence of having an IOLTA, will be in violation of the rules governing the safekeeping of property.

The lawyer may keep upwards of \$500 of her own funds to cover regular bank charges and fees on the account, if any.⁴ If more than \$500 of the attorney's monies is in the account, the lawyer should be prepared to offer an explanation. Any reason other than the regular bank fees and charges on the account are more than \$500, which should be substantiated, will be frowned upon. In addition, the \$500

of funds belonging to the lawyer that are held in the IOLTA must be accounted for and can be replenished as needed. Do not use the IOLTA to shield funds belonging to the lawyer or, for that matter, belonging to the client, from the IRS. The disciplinary regulators will anticipate this as a plausible reason for the attorney holding personal funds in the account, so don't give them cause to be correct.

2. Do Not Hold Funds of a Client/Third Person That They are Entitled to Receive

Upon the termination or conclusion of a client matter, any remaining clients' funds should be promptly returned. While a written accounting is not required in every case, it is always required in contingency fee cases.⁵ It is prudent for the lawyer who is making disbursement of a client's funds to provide the client with a written accounting of all disbursements. The rules require such records be maintained, so provide the accounting in a meaningful way to the client as well. For example, any fees or costs which are billed against a retainer will show payment made from the retainer.

In contingency fee cases, clients must be promptly notified by the lawyer of the receipt of any settlement proceeds.⁶ However, it is the failure to give the client monies due and owing which may result in a reprimand or presentment. The rules governing the delivery of property that belongs to a client or third person are strictly enforced.⁷ This applies to an attorney's failure to timely provide the client, who terminated the relationship, with an accounting and a refund of unearned retainer fees.

Conversely, a lawyer should not avoid the scrutiny that applies to the IOLTA. This means that the law firm should not deposit unearned clients' fees in the operat-

ing account. This issue arises in even the uncontroversial ways. For example, when a client overpays a bill: deposit the funds into a clients' funds account, disburse the proper amount for the legal fee, and then reimburse the excess or apply the remainder to a future billing statement, but only with the client's consent.

More complex issues may arise with regard to real estate and transactional work, but the resolution is no different. Keep the clients' monies properly accounted for and separate from the firm's funds. If there are remaining funds at the conclusion of the matter, which should be evident in the required periodic reconciliations of the accounts, disburse the funds appropriately.

3. Do Not Misappropriate Funds

A misappropriation will lead to a disciplinary presentment. More simply stated, the theft of client monies will result in disbarment, under Practice Book § 2-47A.

Misappropriations may not appear as direct theft of clients' funds when the IOLTA is at issue—but that is what is happening. Bear in mind that while the clients' funds account holds a cumulative amount of money belonging to many clients, the lawyer must know the exact amount held for each client. This is all part of the recordkeeping process. A lawyer who disburses funds from Client A's funds must know how much money Client A has in the IOLTA.

The lawyer cannot disburse monies on behalf of Client A using Client B's funds. If that occurs, the lawyer has misappropriated Client B's funds. It is irrelevant that it is for the benefit of Client A or that the lawyer intends to replace the funds. Also, a lawyer cannot issue a check from the IOLTA to a third person against clients' funds that have not been deposited.

Similarly, a lawyer cannot use the IOLTA to refund an overpayment of legal fees to the lawyer. Nor can a lawyer make an unauthorized loan against the clients' funds.

4. Do Not Ignore Overdrafts

When an overdraft occurs in an IOLTA, the regulatory authorities receive notice of the overdraft from the financial institution. The disciplinary authorities will immediately request an explanation from the lawyer about the overdraft. The attorney must comply. The first strike against the lawyer is that the overdraft strongly suggests that the lawyer has mismanaged the clients' funds that have been entrusted to him. A second strike occurs with the attorney's failure to address and rectify the situation in cooperation with the regulatory authorities. The combination will result in a presentment.

5. Do Not Neglect to Maintain Required IOLTA Records

The Commentary to Rule 1.15 provides for a specific accounting procedure, commonly known as the "three-point reconciliation." The three-point reconciliation is a comparison of the records that include the "trial balance," the "control balance," and the bank statement balance on one given date. These three critical components, which can be simply described as follows, have additional requirements.⁸

Client Ledgers. For each client, there must be a client ledger showing all receipts and disbursements of funds in client A's account, which must include a running balance. When the sum on each individual client ledger is added together, it is referred to as the client ledger "trial balance" on a given date.⁹

General Ledger. The general ledger shows all receipts and disbursements of funds in the IOLTA, and must include a running balance.¹⁰ The general ledger balance, which is the "control balance," is the final balance on the same date as the trial balance is run. It should include all receipt and disbursement entries for transactions as of that date.¹¹

Bank Statement Balance. The bank statement is used as a third check. The bank statement balance is determined by taking the statement balance, subtracting the outstanding checks, and

adding the deposits not credited. Again, the bank statement balance should be done on the same date as the other two checks.¹²

The sums of each should be the same amount.¹³ The three-point reconciliation should be documented. These records must be retained in compliance with Rule 1.15.¹⁴

The lack of proper records can arise in several ways: a random audit by the statewide grievance committee; an ordered audit by the statewide grievance committee, such as in the case of an overdraft notification; or during a disciplinary action where the client is claiming issue with payments made to the lawyer. The sanction of a reprimand combined with restitution and continuing legal education was ordered in one case, but presentments were also ordered. However, the presentment cases do not hinge on the lack of recordkeeping, but rather on other issues addressed in the proceeding. Inadequate law office management practices are likely a symptom and not the cause of other professional discipline problems.

Conclusion

If the reader is surprised by even one of the top five abuses, a review of additional resources may help.¹⁵ The lawyer is the only person responsible for the clients' funds account, even if the administrative tasks are delegated to law firm staff, so act with care. While CLE courses are periodically offered on this topic, the lawyer should simply know and understand the rules governing IOLTAs set forth in Rule 1.15. The requirements for the management and recordkeeping of clients' funds accounts are detailed. Finally, remember it is necessary to register an IOLTA on the Connecticut Statewide Grievance Committee Annual Attorney Registration Form.

There is no infraction by an attorney that casts a wider cloud over the entire profession than misconduct concerning clients' monies. While no amount of knowledge will eliminate intentional conversions, all attorneys should be well versed in the applicable Connecticut Rules of Professional Conduct. **CL**

Notes

1. The *Connecticut Lawyer* periodically includes a compilation of summaries of the statewide grievance committee reported decisions in "The Professional Discipline Digest."
2. Rule 1.15(g). An IOLTA account is defined as an "interest- or dividend-bearing account established by a lawyer or law firm for clients' funds at an eligible institution from which funds may be withdrawn upon request by the depositor without delay." Rule 1.15(a)(5). The client may opt out. Rule 1.15(d).
3. Advance fee payments should be drawn down as agreed upon with the client, but only after the services have been provided and the fees have been earned.
4. Rule 1.15(c).
5. Rule 1.5(c).
6. Rule 1.15(e); *see also* Rule 1.4.
7. Rule 1.15(e) of the Connecticut Rules of Professional Conduct states: "Upon receiving funds or other property in which a client or third person has an interest, a lawyer shall promptly notify the client or third person. Except as stated in this Rule or otherwise permitted by law or by agreement with the client or third person, a lawyer shall promptly deliver to the client or third person any funds or other property that the client or third person is entitled to receive and, upon request by the client or third person, shall promptly render a full accounting regarding such property."
8. Of course, there is no substitute for reading the rules applicable to IOLTAs.
9. *Id.*
10. The general ledger must identify which individual clients' funds account or ledger is affected.
11. *Id.*
12. *Id.*
13. If there is discrepancy, the lawyer must determine the reason and rectify the records or the situation as warranted. If there is a legitimate reason for a discrepancy, make a record of the reason, and reconcile the accounts.
14. The records must be maintained for a period of seven years from the termination of the representation. Rules 1.15(b) and 1.15(i).
15. Kimberly A. Knox, *A Primer on Managing Clients' Funds: The Business Acumen that Law School Fails to Teach*, 22 CONN. LAW. NO. 4, 2011, AT 10.