

Spring trust account cleanup

Spring cleaning is something I always aspire to do but never get around to doing. Even so, I enjoy thinking about all of the ways I could and should get my life together each spring, and I usually manage one or two small projects. Although I have written about trust accounts previously, a string of discipline cases we are handling has inspired me to write again on this important topic. I would like to encourage everyone who is responsible for a trust account (or a partner in a firm who has delegated trust account responsibilities to someone else) to take time this spring to make sure your trust account books and records are in good order.

The basics

One of the most important duties we have as lawyers is to handle the property of others “with the care required of a professional fiduciary.”¹ Minnesota departs substantially from the ABA model rules regarding the safekeeping of property, primarily with regard to the level of specificity in our rule versus the model rule.² The details in our rule and

the appendix provide useful information to help lawyers keep their records in good order; the main requirements, however, are largely the same whether you are looking at the model rule or Minnesota’s rule.

All funds of clients or third parties held by a lawyer in connection with a representation must be deposited into an approved IOLTA account.³ This is not negotiable. For example, if a client pays you an advance to cover expenses to be incurred in the

matter, those funds must go into trust. If a client provides you with funds to use to pay a third party in settlement of a dispute, those funds must go into trust. If you receive funds in settlement of a client’s dispute, those funds must go into trust. Failure to place and maintain those funds in trust will lead to discipline.

The only exception to the above is the circumstance where a client pays an expense by credit card. Many credit agreements require you to agree that charges can be reversed under certain circumstances. That can be dangerous in a trust account (such as where a credit card company backs out a charge months later), so it is permissible to initially deposit credit card payments in your business account, but then you must immediately transfer the required funds into trust.⁴ That way, if the charge is later reversed, the money is taken from your business account, and does not result in the inadvertent misappropriation of funds from the trust account if you have already disbursed the original sum.

All fees received in advance of legal services being performed must be placed in trust and not withdrawn until earned, with one exception.⁵ Again, this is a bright line requirement and non-negotiable. Placing advanced, unearned fees into your business account (absent a compliant flat or availability fee agreement as discussed below) means you are failing to safe-keep property of your client, a violation of Rule 1.15(a). And worse, if you then spend those funds before they are earned, you have misappropriated the funds of others.

The only exception to this requirement is found in Rule 1.5 (fees). If you charge a flat fee or an availability fee under circumstances compliant with the rule, you may put that fee into your business account, and treat it as your property subject to refund.⁶ The Office enforces strict compliance with the requirements of Rule 1.5 given that it is an exception to an important safekeeping requirement. If you use flat fees or availability fees, read carefully the requirements of Rule 1.5 to ensure you have a written, signed agreement consistent with the ethics rules before placing fees not yet earned into your business

account. Too many people receive discipline each year for violations of this requirement.

Books and records

Now that the very important basics are covered, let’s review the books and records requirements. Many of these requirements are set forth in Appendix 1 to the MRPC, and are in place to make sure lawyers on a monthly basis are keeping good track of client funds to prevent the mishandling of those funds. Some highlights include:

Lawyers must sign every trust account check and direct every electronic transfer.⁷ Do not delegate signing trust account checks to office staff or your accountant. Withdrawals by electronic transfer should also be documented by written memorandum signed by the attorney responsible for the transfer.⁸

Earned funds must be withdrawn within a reasonable time of being earned, and a written accounting of all such withdrawals must be provided to the client.⁹ Do not commingle earned funds in trust. You can and should keep a nominal amount of your own funds in trust (no more than \$200) to cover unexpected bank charges, but do not otherwise leave earned fees in trust longer than the next billing cycle.

Make sure you or someone who knows the rules well is performing a monthly *three-way* reconciliation of your trust account.¹⁰ You need to reconcile your trial balance report, your check register, and your bank statement balance—adjusted for outstanding deposits and withdrawals—every month. This is not how accountants or bookkeepers typically think about reconciliation, because generally accepted accounting principles do not require client subsidiary ledgers or monthly trial balance reports, but trust accounts do.¹¹ Do this every month, and maintain a copy of your work.¹² Doing this monthly helps you catch mistakes. Mistakes happen, and as long as you catch them within the next month, you are unlikely to have an issue with discipline. Where issues arise is where attorneys do not do this monthly, a mistake happens, and it persists for months on end because they are not doing the required work.



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If you accept cash, make sure you provide a receipt countersigned by the client and keep a copy.¹³ A lot of disputes are easily avoided by this simple act.

Retain your books and records for six years following the tax year to which they relate.¹⁴ Make sure you have effectively backed up all of your records as well, so that you can satisfy this rule.

Do not disburse funds until they have cleared the issuing bank.¹⁵ This is materially different from the date the funds post to your account and are available for disbursement. You put other people's money at risk when you do this, and it is one of the reasons we get several overdraft notices a month from banks.

Make sure your firm has in place effective measures to ensure compliance with these rules. Every lawyer is ethically responsible for the correct handling of his or her own client's funds, whether they are in solo practice or a firm. You can delegate some of these duties, but it is then your responsibility to ensure that those to whom the task has been delegated perform the work correctly.¹⁶

Recently, we have seen a number of cases where lawyers in small firms relied upon a bookkeeper or other designated individual to handle their trust account records, and thought everything was fine when it was not. As the licensed attorney, you are responsible.

Resources

The Office has several resources available on its website to assist lawyers to meet their trust account obligations, including a brochure, *Other People's Money: Operating Lawyer Trust Accounts* (2015), and a list of frequently asked questions about trust accounts. We have also added new links at our website to two MSBA resources, *IOLTA Guide*, *QuickBooks Online* (2017) and *IOLTA Guide—CosmoLex* (2016), with the MSBA's permission. And remember you can always call the OLPR for an advisory opinion (651-296-3952 or 1-800-657-3601) on specific trust account questions. We want you to get this right, so please let us know how we can assist. Good luck with your spring trust account cleanup! ▲

Notes

Rule 1.15(a), Minnesota Rules of Professional Conduct (MRPC), Comment [1].

² Rule 1.15, MRPC, and Appendix 1, MRPC, compare ABA Model Rule 1.15.

³ Rule 1.15(a), MRPC.

⁴ Appendix 1, MRPC, I(10).

⁵ Rule 1.15(c)(5), MRPC.

⁶ Rule 1.5(b)(1), MRPC; Rule 1.5(b)(2), MRPC.

⁷ Rule 1.15(j), MRPC.

⁸ Rule 1.15(h), MRPC, Appendix 1 I(6).

⁹ Rule 1.15(b), MRPC.

¹⁰ Appendix 1, MRPC, I(5).

¹¹ Appendix 1, MRPC, I(3)(a), I(4).

¹² Appendix 1, MRPC, I(7).

¹³ Appendix 1, MRPC, II(2).

¹⁴ Rule 1.15(h), MRPC.

¹⁵ Appendix 1, MRPC, I(11).

¹⁶ Rules 5.1, 5.2 and 5.3, MRPC.

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