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7 Tips for Trustworthy Trust Accounting

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SMART BUSINESS STRATEGIES FOR THE LEGAL WORLD.

Presenter



- ▶ **Partner, Affinity Consulting Group**
- ▶ **Law firm consultancy focused on helping law firms implement technology, finance, marketing and management solutions**
- ▶ **Worked in a law firm as an Administrator performing the billing and accounting functions**
- ▶ **25 years experience with law firm billing and accounting**

What is a Lawyer's Trust Account

Operating Account



YOUR MONEY

Trust Account



NOT YOUR MONEY

IOLTA/COLTAF

Interest on Lawyer's Trust Account and it benefits the Colorado Lawyer Trust Account Foundation

Professional Rules of Conduct Rule 1.15A(2)

If a lawyer or law firm participates in Interest on Lawyer Trust Account ("IOLTA") programs in more than one jurisdiction, including Colorado, IOLTA funds that the lawyer or law firm holds in connection with the practice of law in Colorado should be held in the lawyer or law firm's COLTAF account (as defined in Rule 1.15B(2)(b)). The lawyer or law firm should exercise good faith judgment in determining which IOLTA funds it holds in connection with the practice of law in Colorado.

Types of COLTAF accounts

Rule 1.15E(c)(8)

- ▶ A COLTAF account may be established by a lawyer or law firm and a financial institution as:
 - ▶ (A) A checking account paying preferred interest rates, such as market-based or indexed rates;
 - ▶ (B) A public funds interest-bearing checking account, such as an account used for other non-profit organizations or government agencies;
 - ▶ (C) An interest-bearing checking account, such as a negotiable order of withdrawal (NOW) account, or business checking account with interest; or
 - ▶ (D) A business checking account with an automated investment feature in overnight daily financial institution repurchase agreements or money market funds.

Trust Accounting

- ▶ **Staff may assume tasks but not duty.**
- ▶ **Duty is accomplished by having at least two bank accounts**
 - ▶ Operating (Firm's money)
 - ▶ IOLTA/Trust (Client money)

What Goes in Trust

- ▶ **Settlement funds**
- ▶ **Refundable Fee Retainers/Advances of unearned Fees**
- ▶ **Funds owed to lienholders**
- ▶ **Advances for costs not yet incurred**
- ▶ **Amounts in dispute**
- ▶ **Real Estate Closing Funds**
- ▶ **NOMINAL firm funds to cover bank fees**

What Does NOT Go in Trust

- ▶ **Firm's Business Funds**
- ▶ **Payroll Monies;**
- ▶ **Lawyer's Personal Funds**
- ▶ **Fixed Fees or Advanced Payment Retainers**

Rule 1.15B(b)

One or more of the trust accounts may be a Colorado Lawyer Trust Account Foundation ("COLTAF") account. A "COLTAF account" is a **pooled trust account** for funds of clients or third persons that are nominal in amount or are expected to be held for a **short period of time**, and as such would not be expected to earn interest or pay dividends for such clients or third persons in excess of the reasonably estimated cost of establishing, maintaining, and accounting for trust accounts for the benefit of such clients or third persons. **Interest** or dividends paid on a COLTAF account shall be **paid to COLTAF**, and the lawyer and the law firm shall have no right or claim to such interest or dividends.

Where to Deposit Trust Retainers

- ▶ Reasonable judgement re: will client's funds bear significant interest
- ▶ Else – IOLTA (pooled) trust account;



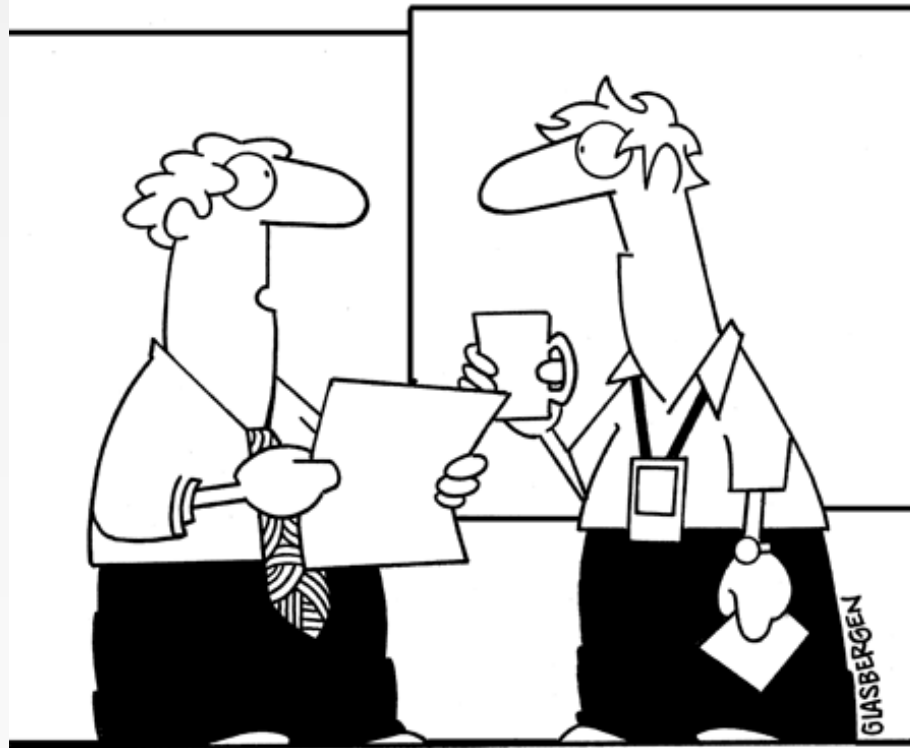
Overdrawing the Trust Account

- ▶ **Authorized Banking Institutions must report overdrafts to the Regulation Counsel**
- ▶ **Avoid mistakes by using legal profession software to properly maintain attorney trust accounts**
- ▶ **If overdraft occurs, document and correct immediately.**



TOP 7 MISTAKES TO AVOID WITH LAWYERS' TRUST ACCOUNTS

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**“We need to prepare for our audit.
Organize a game of dodge ball!”**



**KEEP
CALM
AND
TAKE THE
RESPONSIBILITY**



**NOT UNDERSTANDING &
LACK OF RESPONSIBILITY**

Solution

1

- ▶ **Consider mailing the bank statement to your home address, not the office**
- ▶ **Instruct staff to deliver to attorney**
- ▶ **Log-in and download/print/review statement**
- ▶ **Review Trust Ledger balances**
- ▶ **Do it religiously**
- ▶ **Delineate staff responsibilities clearly**
- ▶ **Protect the check stock**

- ▶ **Did you know that most states require the firm to sign a Trust Accounting Certificate each year certifying they are in compliance?**
- ▶ **Are you confident your firm complies with these requirements?**

2

NOT UNDERSTANDING 3-WAY RECONCILIATION PROCESS & REPORTS



What is 3-Way Reconciliation

2

- ▶ **Accounting Books Journal Balance;**
- ▶ **Actual Bank Account Balance;**
- ▶ **Client Ledger Balance.**

Solution

2

- ▶ **Learn/review 3-way reconciliation**
- ▶ **If necessary, learn manual reconciliation**
- ▶ **Do it faithfully each month**
- ▶ **Use SOFTWARE made for law firms**

Three-way reconciliation example

CALCULATED STATEMENT BALANCE
 BANK STATEMENT BALANCE
 DIFFERENCE

128556.17
 128556.17
 0.00

*** Bank Journal Reconciliation ***

Jul 31/2009 ENDING BALANCE ON BANK STATEMENT

128556.17

TOTAL OUTSTANDING CHECKS

22752.96

-22752.96

*** Outstanding Receipts ***

00041	05-018	415.00
01130	09-078	1250.00
01140	09-209	229.00

TOTAL OUTSTANDING RECEIPTS

+ 1890.00

CALCULATED BANK JOURNAL BALANCE
 ACTUAL BANK JOURNAL BALANCE
 DIFFERENCE

107693.21
 107693.21
 0.00

Client	Client Name	Description	Resp Lwyr	Bank Acct#	Acct Balance	Last Trust
893	Naples, Florida 34119					
	08-354	Foreclosure	EWH	1	1462.50	Jul 29/2009
718	Naples, FL 34109					
	08-166	Foreclosure	EWH	1	950.00	Jul 29/2009
Firm Totals: 1 - Trust Bank Account 1					107693.21	

3

IMPROPER USE OF TRUST ACCOUNTS

	Next
ACCOUNT BALANCE	
06	\$1,875.21
08	\$2,207.07
10	\$5,743.05
12	\$8,419.05
01	\$6,487.61
02	\$11,968.53
03	\$13,968.53
04	\$14,416.72
05	\$9,416.72
06	\$9,431.22
07	\$9,670.32
08	\$9,768.24
09	\$10,068.24
10	\$11,081.61
11	\$11,381.61
12	\$14,896.08
01	\$12,263.26
02	\$12,336.26
03	\$7,336.26
04	\$7,363.96
05	\$7,532.51
06	\$7,654.98
07	\$7,864.98
08	\$9,372.19
09	\$20,785.84
10	\$13,336.26
11	\$9,416.72
12	\$9,431.22
01	\$9,670.32
02	\$9,768.24
03	\$10,068.24
04	\$11,991.61
05	\$11,381.61
06	\$14,800.08
07	\$9,632.22

Solution

3

- ▶ **IOLTA/CLIENT - Refundable Retainer**
- ▶ **Advanced Payment Retainer**
- ▶ **Understanding/purpose for the deposit of funds to trust – in writing**
- ▶ **Where to deposit funds?**
- ▶ **Approved Banking Institution**
- ▶ **Responsibility and Accountability is with the lawyer**
- ▶ **Keeping earned fees in the account**



4

RECORD RETENTION DUTIES

Solution

4

- ▶ **Keep detailed records for 7 years after representation ends**
- ▶ **Start timer when file is closed**
- ▶ **Never close a file with a trust balance**
- ▶ **Record prompt return of funds**
- ▶ **Verify no outstanding items**

5

UNCLAIMED FUNDS



Solution

5

- ▶ **Void outdated outstanding items**
- ▶ **Reissue new check**
- ▶ **Communicate with client**
- ▶ **Locate owner of the funds**
- ▶ **Make periodic reasonable efforts to find fund owners**
- ▶ **Issue a cashier's check?**
- ▶ **Issue unclaimed funds to COLTAF**

A man in a blue shirt is looking up with a distressed expression, his hand on his forehead, surrounded by towering stacks of papers and folders. The stacks are blurred in the background, emphasizing the overwhelming amount of information. In the top right corner, there is a grey circle containing a red number 6.

6

IMPROPER DOCUMENTATION & STORAGE

Solution

6

- ▶ Document source of funds
- ▶ Preserve signed authorizations
- ▶ Track purpose for holding the funds
- ▶ **DOUBLE CHECK** name printed on checks
- ▶ **DOUBLE CHECK** name on the account
- ▶ Verify and re-verify wiring instructions – rampant bank wire fraud

Reporting Requirements

6

Here is where Law Firm accounting software makes a difference!

- ▶ **Separate ledger for each client/matter itemizing every transaction for that matter**
- ▶ **Copies of deposit slips**
- ▶ **Original or legible copies of cancelled checks**
- ▶ **Separate trust receipts and trust check journal reports identifying date, client and matter, check or receipt number, explanation, and amount**
- ▶ **Bank statements and reconciliation reports showing outstanding items**

Sample Client Ledger

Jun 9/2010

Melfa, Plashkes & McMurray, LLP
 Client Trust Ledger
 To Jun 9/2010

Client		Resp		Bank		Last Entry	
Matter	Description	Lawyer	Bank	Deposit	Receipt	Disbs	Acct Bal
Date	Received From/Paid To	Che#/Rec#	Acct#	Type			
Entry #	Explanation						
2327	Walters, Kenneth	AJC					
2327-001	Walters vs. Collier County - Slip and fall at the Collier County Courthouse						Apr 15/2010
Apr 14/2010	ABC Insurance company	00042	1	Check	100000.00		100000.00
3504	Settlement						
Apr 14/2010	Melfa, Plashkes & McMurray, LLP	1264	1			40905.50	59094.50
3529	Trust transfer						
Apr 15/2010	Collier County Anesthesiologists	1265	1			3750.00	55344.50
3544	Invoice 7898 Final Payment						
Apr 15/2010	Naples Community Hospital	1266	1			14236.99	41107.51
3546	Full and Final Payment for Kenneth Walters A/C 2936-						
Apr 15/2010	Kenneth Walters	1267	1			41107.51	0.00
3548	Settlement Proceeds						
Matter Total:			1		100000.00	100000.00	
Client Total:			1		100000.00	100000.00	
Firm Totals: 1 - IOTA Trust, Bank of America, 23526022					100000.00	100000.00	





**ONE "TRUSTED" PERSON
DOES IT ALL**

➔ Florida Law Firm Office Manager Charged In \$1.67 Million Theft



[REDACTED] Florida, was arrested yesterday and charged with stealing some \$1.67 million from the now defunct law firm of [REDACTED]. [REDACTED] was charged with 259 felony counts in connection with the alleged theft - specifically, 129 counts of grand theft, 114 counts of wire fraud and 16 counts of writing forged checks, and two misdemeanor counts of petty theft. The embezzlement occurred since 2002 when she was hired by the law firm whereby [REDACTED] would deposit firm checks or wire transfer company funds into her own personal accounts.

Solution

7

- ▶ **The potential for embezzlement exists**
- ▶ **The ultimate responsibility is with the lawyers**
- ▶ **Asking questions is critical**
- ▶ **Transparency is KEY**

Trust Account Mistakes Investigated

- ▶ **Trust account check issued against uncollected funds (post-dated check syndrome);**
- ▶ **Deposited item is returned;**
- ▶ **Online computer banking errors (Person mistypes information);**
- ▶ **Telephone banking errors (e.g., teller/backroom personnel credit items into a different account);**
- ▶ **Using the trust account for personal, not client trust, purposes;**
- ▶ **Calculation errors on settlements or closings;**
- ▶ **Using the wrong check book; and**
- ▶ **Insufficient internal procedure for wire verification**

Disbursement of Funds (FL example)

The lawyer may disburse collected funds in reliance on these deposits due to a limited and acceptable risk of failure:

- ▶ Certified check or cashier's check
- ▶ Loan proceeds from a federally or state chartered bank, S&L Assn., Credit Union, etc.
- ▶ Bank check, official check, treasurer's check, money order or other bank issued instrument
- ▶ Trust account check from another lawyer in FL or escrow account of a licensed FL real estate broker
- ▶ US or State of Florida issued check
- ▶ Check or draft from an insurance co., title ins. company

Credit Cards?

- ▶ **Should you allow them for the Trust Account?**
- ▶ **Rely on a vendor that understands law firm requirements (LawPay, LawCharge)**
- ▶ **ALL processing charges MUST come out of the Operating Account**
- ▶ **Client gets credit for the FULL deposit**

Conclusion

- ▶ **Read and understand ABA and Colorado Rule 1.15**
- ▶ **Use Accounting Software made for Lawyers**
- ▶ **Don't entrust Trust to one employee Only – maintain oversight**
- ▶ **If you make a mistake, rectify immediately**



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QUESTIONS?

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