Client Trust Accounting for Arizona Attorneys

Publication of the State Bar of Arizona

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The State Bar's Lawyer Regulation Office and Special Services Department have prepared this Client Trust Accounting Manual for Arizona Attorneys for its members. It has not been adopted or endorsed by the State Bar's Board of Governors, and does not constitute the official position or policy of the State Bar of Arizona. It is advisory only and is not binding on the Arizona Supreme Court.

The Manual contains legal information, not legal advice. While the State Bar will make every effort to update the manual as necessary, it is the responsibility of members to make sure that they are following the most current version of the Arizona Supreme Court Rules, which contain the Arizona Rules of Professional Conduct, in conjunction with this manual. Nothing contained in this Manual is intended to address any specific legal inquiry, nor is it a substitute for independent legal research to original sources or for obtaining the advice of legal counsel with respect to legal problems.

Acknowledgements

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The State Bar of California, *Handbook on Client Trust Accounting for California Attorneys* © 2006 *(For the current online version of the California Handbook, please go to:* http://www.calbar.ca.gov/calbar/pdfs/ethics/2006_CTA_Handbook.pdf)
at State Bar of Arizona Trust Account Manual Section I, Pages 2-3, Section II, Pages 6-26, Section III, Pages 27-32, Section IV, Pages 33-40, Section VI, Pages 47-49, Section VII, Pages 54-56, Section VIII, Pages 59-70, and Section IX, Pages 72-83.

Colorado Bar Association, *Summary of Trust Account Concepts and Procedures* 2007, at State Bar of Arizona Trust Account Manual Section I, Pages 4-5 and Section VI, Pages 52-53.

David E. Johnson, Jr., Esq., *Trust and Business Accounting for Attorneys* © 2008. All rights reserved
at State Bar of Arizona Trust Account Manual Section IV, Pages 41-42, Section VI, Page 51, and Appendix B, Pages B1-B3 and B10.

Minnesota State Bar Association, *Other People's Money: Operating Lawyer Trust Accounts,* 2010. (*Available online at:* http://www.mncourts.gov/lprb/OtherPeoples$$.pdf) at State Bar of Arizona Trust Account Manual Section XIV, Page 107.

North Carolina State Bar, *Attorney's Trust Account Handbook,* 2009. (*Available online at:* http://www.ncbar.gov/PDFs/Trust%20Account%20Handbook.pdf) at State Bar of Arizona Trust Account Manual Appendix C, Pages 1-2.

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Table of Contents

	Introduction	1
Section I:	The Importance of Client Trust Accounting	2
Section II:	The Rules	6
Section III:	Key Concepts in Client Trust Accounting	27
	A. Separate Clients Are Separate Accounts	27
	B. You Can't Spend What You Don't Have	27
	C. There's No Such Thing As a Negative Balance	28
	D. Timing Is Everything	28
	E. You Can't Play the Game Unless You Know the Score	29
	F. The Final Score Is Always Zero	30
	G. Always Maintain an Audit Trail	31
Section IV:	Opening a Client Trust Account	33
	A. General Do's and Don'ts	33
	B. "IOLTA" Accounts	35
	C. Know Your Bank	35
	D. Who Must Maintain a Trust Account	36
	E. Approved Depositories For Trust Funds	36
	F. IOLTA or Separate Trust Account?	37
	G. Account Names	40
	H. Proper Signatories	41
	I. Responsibility For Establishing and Maintaining Proper Trust Accounts	42
	J. FDIC Insurance	42
	K. Is Help Available?	43
	1. www.azbar.org	
	2. Foundation Website – www.azflse.org	
	3. Ethics Hotline	
	4. LOMAP	
	5. Online Trust Account CLEs	
	6. Trust Account Hotline	

Section V:	**Fees**	**44**
	A. Advanced Fee	44
	B. Flat Fee	44
	C. Retainer	44
	D. Advanced Fees and Costs	45
	E. Contingent Fees	46
Section VI:	**Depositing Money into Your Client Trust Account**	**47**
	A. What MUST go into your client trust account?	47
	B. What MAY go into your client trust account?	47
	C. What MUST NOT go into your client trust account?	49
	D. What about credit card payments?	49
	E. Limited-Risk Deposit Exceptions	50
	F. Disputes With a Client	50
	G. Disputes With Third Parties Over Funds in a Trust Account	51
	H. Third-Party Claims to Funds in a Trust Account	51
Section VII:	**Paying Money Out of Your Client Trust Account**	**53**
	A. What payments CAN you make?	53
	B. What payments CAN'T you make?	53
	C. How MUST you make payments?	54
	D. Who SHOULD make payments?	54
	E. When MUST you make payments?	54
	F. Check 21	55
Section VIII:	**Recordkeeping**	**59**
	A. How long must YOU keep records?	61
	B. Where MAY you keep your records?	61
	C. What if you HAVE a computerized system?	61
	D. Which bank created records do YOU have to keep?	62
	E. How SHOULD you file bank created records?	62
	F. What records do YOU have to create?	62
	G. Automated Alternatives to Managing Your Trust Account	66
	H. What records do YOU have to keep of other properties?	69
	I. Other Resources	69
	J. Reminders	70

Section IX:	**Reconciliation**	**71**
	A. Reconcile the General Ledger/Checkbook Register with the Client Ledgers	79
	B. Reconcile the General Ledger/Checkbook Register with the Bank Statement	79
	C. Calculate the Adjusted Balance	82
	D. Trust Reconciliation Sheet	82
Section X:	**Internal Controls**	**83**
	A. The Need For Control	83
	B. Diversification of Financial Functions	83
	C. Exercising Control of Records	84
	D. Exercising Control Over Employees	85
	1. Hiring	
	2. Instruction	
	3. Supervision	
	E. Process	86
	F. Billing Clients Regularly	86
	G. Separate Trust Accounts For Lawyers in Same Firm	86
	H. Insurance – The Ultimate Control	86
Section XI:	**Random Trust Account Examinations**	**88**
Section XII:	**Other Relevant Trust Account Topics**	**89**
	A. Abandoned Property/Funds	89
	B. Trust Account Overdraft Notification	90
	C. Closing a Client Trust Account	91
	D. Death or Disability and the Client Trust Bank Account	92
	E. Fraud	94
	F. Credit Cards and IRS Section 6050W	97
Section XIII:	**The Mechanics of a Trust Account Investigation**	**98**
	A. Why the Investigation Begins	98
	B. What Happens During the Examination	99
Section XIV:	**Frequently Asked Questions**	**102**

Appendices

Appendix A: Arizona Rules of Professional Conduct, Rule 42, ER 1.15 and Rule 43, Ariz. R. Sup. Ct.

Appendix B: Example Forms

A. Deposit Slip for One Client	B-1
B. Deposit Slip for Multiple Clients	B-2
C. Deposit Log	B-3
D. Trust Account Check	B-4
E. Individual Client Ledger	B-5
F. Administrative Funds/Bank Charges Ledger	B-6
G. General Ledger	B-7
H. Checkbook Register	B-8
I. Three-Ring Trust Checkbook	B-9
J. Three-Way Reconciliation	B-10
K. Sample Fee Agreements	B-11
L. Types of Fees	B-12
M. Explanation of Fee Agreement Terms	B-14
N. Sample Contingent Fee Agreement	B-17
O. Sample Hourly Fee Agreement	B-20
P. Sample Flat Fee Agreement	B-23
Q. Sample Flat Fee and Hourly Agreement	B-25
R. Sample Miscellaneous Fee Agreement Provisions	B-28
S. Notice to Financial Institution, Instructions, Enrollment Form	B-35

Appendix C: Practical Suggestions from State Bar Trust Account Examiners

Introduction

Trust account.

These two words can send chills up and down the spines of new and experienced lawyers alike. Fear of making a mistake. Fear that you haven't trained your staff well enough. Fear that you don't understand the rules.

And besides that, you didn't go to law school to become an accountant, did you?

We put together this handbook to help dispel those fears. We've heard your questions and concerns at seminars and on the State Bar's ethics and trust account hotlines. We've seen your mistakes through trust account examinations. We know the errors that often result in discipline for trust account violations.

Not only does this handbook explain the *how-tos* of trust accounts but we also explain the *whys* of trust accounts. We also address a variety of trust-account-related issues.

A couple of general tips as you read this handbook and use it as a resource.

First, always remember that it's not your money. That's why it's in a trust account and not your operating account.

Second, your trust account must never have a negative balance. A negative balance means a serious problem.

Third, you should always know to whom the money in your trust account belongs. You can have mystery money in your operating account – *hey, an extra $100 I didn't realize I had until I balanced the account!* – but not in your trust account.

Finally, you must have a detailed paper trail for everything concerning your trust account.

We hope this handbook answers all of your questions – including questions you didn't realize you had until you read it – and provides a guide for accurate and ethical client trust accounting.

And you don't even have to be an accountant to get it right.

SECTION I: THE IMPORTANCE OF CLIENT TRUST ACCOUNTING

If you became disabled or died suddenly, would your clients – or the personal representatives of your estate – be able to tell how much of the money in your client trust account belonged to each client? If a State Bar investigator asked you to account for a particular client's money, would you be able to do so? Would the investigator find complete, systematic, up-to-date records showing what's been received and paid out for each client, or would the investigator find a random assortment of canceled checks, unopened bank statements, and general ledgers/checkbook registers full of cryptic notations and rounded-off figures? In these situations, the fact that you "have it all in your head" isn't going to help your clients find their money or satisfy the State Bar.

There are two completely mistaken preconceptions about client trust accounting. One is that client trust accounting is a mysterious, complicated process that requires years of training and innate mathematical ability. The other is that "maintaining a client trust account" simply means opening a bank account and depositing clients' funds into it.

The truth is that client trust accounting consists of a simple set of easy-to-learn and easy-to-use procedures that require consistent, careful application. But as simple as it is, client trust accounting still means more than keeping money in the bank. A bank account is something you have; client trust accounting is something you *do* in order to know—and to show your clients that you know—how much of the money in your account belongs to each client.

Whether you find it easy or difficult, the fact is that if you agree to hold money in trust, you take on a non-delegable, *personal* fiduciary responsibility to account for every penny as long as the funds remain in your possession. This responsibility can't be transferred, and isn't excused by your ignorance, inattention, incompetence or dishonesty, your employees' or your associates'. The legal and ethical obligation to account for those monies is yours and yours alone, regardless of how busy your practice is or how hopeless you are with numbers. You may employ others to help you fulfill this duty, but if you do, you must provide adequate training and supervision. Failure to live up to this responsibility can result in personal monetary liability, fee disputes, loss of clients and public discipline.

The essence of client trust accounting is contained in those three words:

> **Client** (These duties arise in the context of an lawyer-client relationship, regardless of whether you are paid for your services, and are as inviolable as your duty to maintain client confidences. These duties may also be owed to third parties.)
>
> **Trust** (The willingness of people to trust a complete stranger with money just because the stranger is a lawyer is a fundamental aspect of the lawyer-client relationship, and maintaining that trust is the duty of every individual lawyer

and a matter of supreme public interest.)

Accounting (The way to fulfill your clients' trust is to be able, at any time, to make a full and accurate accounting of all money you've received, held and paid out on their behalf.)

That's all "client trust accounting" means. If you follow the simple procedures explained below, you will never have to worry about failing to live up to your duties as a fiduciary no matter how complex or busy your practice is.

Imagine how you'd feel if you asked your bank how much money was in your personal account, and the bank officer explained that the bank couldn't tell you because business was booming and keeping exact records of so much money for so many people would just take too much time. You'd probably feel that if knowing how much of your money it held was too much trouble, the bank shouldn't be holding your money. That's exactly how your clients feel about you. You keep records so you can give your clients an accounting of their money; failing to do so is a violation of your professional responsibilities.

The minute you *don't* keep track of a client's money, you violate the client trust accounting rules. The longer you don't know, the more violations you're likely to stumble into, and if you keep stumbling, sooner or later you're going to stumble into a State Bar investigation.

And don't think if you keep enough of your own money in the client trust account that everything's all right. *Not only does that not satisfy your professional responsibility to your clients, it may also constitute an additional violation known as "commingling."* In short, the only adequate way to fulfill your fiduciary responsibility to your clients is to keep track of how much of their money you have in your client trust account, at all times.

You must maintain a ledger, or the equivalent, for each client that reflects all transactions related to that client's funds, even if you hold money only long enough for the check to clear then disburse and close the matter. If you hold administrative funds to cover the costs of maintaining the account, you also must create a ledger or equivalent for those administrative funds. (This handbook tells more about administrative ledgers in section VIII, page 64.)

Maintaining a common client trust bank account in which the funds of more than one client are held is fine, as long as you keep an accurate record of what belongs to each client. That's what client trust accounting is all about.

Pointers for everyday trust account management

- Do not sign blank trust account checks. If you do, you risk someone using them for improper purposes.

- Do not allow your staff to use a signature stamp. If you do, you risk someone endorsing checks for improper purposes.

- Receive trust account bank statements unopened or sent directly to you by electronic transmission. You can then review the statement before someone could tamper with it.

- Checks on the trust account should never be made payable to "cash." Checks from the trust account should never be used for the lawyer's personal expenses.

- If you delegate duties, do not allow the same person to handle everything to do with the trust account. The person who takes in the deposits should not be the same person who writes the checks on the account.

- Use different colored checkbook covers for your trust account and your operating account so as not to confuse the two when you are in a hurry.

- DO NOT carry your trust account checkbook with you when you leave your office. Many lawyers have written checks for inappropriate disbursements from the trust account "because it was the only checkbook I had with me." The only exception may be when you are making a trip specifically to disburse funds (such as a filing fee) on behalf of the client, but you do not know the exact amount. Before leaving the office, make sure you know exactly how much money is available for that particular client (the checkbook alone will not give you that information if you have money in the account for more than one client) and do not exceed that amount.

- Include in your fee agreement information about how fees will be handled, including money paid in advance for fees or costs and expenses. It's also a good idea to provide your client with an itemized statement of work performed prior to transferring fees that you consider earned. If the client disputes the amount, you will need to hold it in the trust account pending resolution.

- Develop and memorialize a standard procedure for notifying clients or third parties when you receive funds in which they have an interest and take steps to assure that you consistently follow the procedure. Be sure part of the procedure is documenting notice to the client. If it's done by telephone call rather than in writing, be sure to include details of when the call was made and with whom the caller spoke.

- If support staff helps you maintain your trust account, you MUST properly train and supervise them; no matter how long they've been in your employment and no matter how well you believe they understand trust account requirements. Be sure you understand the process well enough to determine if it's being handled

properly.

- Do not set up overdraft protection or a credit line on your trust account. This will be considered commingling of your personal funds if either takes effect.

SECTION II: THE RULES

Read Rule 43, Ariz. R. Sup. Ct. Read it again every year before you sign the annual certificate of compliance that appears on your dues statement. While you've got the book open, read ER 1.15, which deals with the safekeeping of property.

Rule 43 is the roadmap for client trust accounts. Let's go paragraph by paragraph and discuss the rule.

What Rule 43(a) says:

Duty to Deposit Client Funds and Funds Belonging to Third Persons; Deposit of Funds Belonging to the Lawyer. Funds belonging in whole or in part to a client or third person in connection with a representation shall be kept separate and apart from the lawyer's personal and business accounts. All such funds shall be deposited into one or more trust accounts that are labeled as such. The location of the trust account shall be controlled by the provisions of ER 1.15(a). No trust account required by this rule may have overdraft protection. No funds belonging to the lawyer or law firm shall be deposited into a trust account established pursuant to this rule except as follows:

> 1. Funds to pay service or other charges or fees imposed by the financial institution that are related to operation of the trust account, but only in an amount reasonably estimated to be necessary for that purpose may be deposited therein.
>
> 2. Funds to pay merchant fees or credit card transaction charges or to offset debits for credit card chargebacks, but only in an amount reasonably estimated to be necessary for those purposes may be deposited therein.
>
> 3. Earned fees and funds for reimbursement of costs or expenses may be deposited into a trust account if they are part of a single credit card transaction that also includes the payment of advance fees, costs or expenses and the lawyer does not use a credit card processing service that permits the lawyer to direct such funds to the lawyer's separate business account. Any such earned fees and funds for reimbursement of costs or expenses must be withdrawn from the trust account within a reasonable time after deposit.
>
> 4. Funds belonging in part to a client or third person and in part presently or potentially to the lawyer or law firm must be deposited therein, but the portion belonging to the lawyer or law firm must be withdrawn when due and legally available from the financial institution, or within a reasonable time thereafter, unless the right of the lawyer or law firm to receive it is disputed

by the client or third person, in which event the lawyer shall comply with ER 1.15(e).

Some tips about Rule 43(a):

"Funds belonging in whole or in part to a client or third person" requires the lawyer to determine to whom funds belong at the time they are received. The answer to the question of ownership doesn't hinge on the amount of money received or whom that money will belong to tomorrow or next week. For example, some lawyers believe that if the amount of money received is small (some set an arbitrary limit), there is no reason why it has to go into a trust account. Others believe that if they will earn all or most of the money within the next week anyway there is no point in making a trust account deposit and a subsequent transfer to an operating account. Neither assumption is correct.

Generally, three types of funds that should go into a trust account:

- Money belonging entirely to a client, such as a judgment or an advance fee for services the lawyer will perform at some point in the future;

- Money belonging in part to the client and in part presently or potentially to the lawyer, such as a settlement for a personal injury case that will be disbursed to the client and to the lawyer for fees;

- Money belonging to a third party, directly related to representation of a specific client, such as a settlement for a personal injury case that will be disbursed in part to a medical provider.

Some other types of funds received should **not** go to a trust account:

- Money belonging entirely to the lawyer, such as payment for services already performed and billed;

- Payment of an amount that has been designated in a fee agreement as earned on receipt (which defines the funds as belonging to the lawyer when paid by the client) or an amount designated as an earned on receipt flat fee for a particular body of work such as preparation of a simple will.
    - NOTE: Some lawyers believe they must deposit amounts that are clearly designated as earned on receipt to their client trust account because they may need or wish to refund some of the money even though it is designated as "non-refundable." This handbook will not attempt to address ethical issues related to "non-refundable" retainers or to the "reasonableness" of fees in particular circumstances. Lawyers are encouraged to seek

guidance from the State Bar ethics counsel or from the Committee on the Rules of Professional Conduct (Ethics Committee), if appropriate. From a management standpoint, a lawyer may wish to hold aside funds in an account other than the trust account so those funds will be available if the lawyer feels the fee taken was not reasonable under the circumstances or for other reasons, such as when the lawyer chooses to refund money that had been designated at the outset as the lawyer's own.

- Money that is not being held in connection with representation of a client, other than administrative funds as described earlier in these materials. For example, some lawyers act as officers in professional organizations. Those who serve as treasurers may collect money belonging to third parties, such as members who pay dues. Although the lawyer may regard him- or herself as having a fiduciary responsibility to the organization, these duties do not stem from representation of a client on whose behalf funds are being held. Therefore, the lawyer should not keep these funds in the trust account. Likewise, some lawyers act as the repository for monies paid by those in an office-sharing arrangement for various costs and expenses. These types of monies likewise should not be kept in the client trust account.

- The client trust account must be totally separate from accounts in which the firm's operating funds or a lawyer's personal money is kept.

- "[L]abeled as such" means the client trust account checks should bear the notation "IOLTA account," "client trust account," or a similar designation. In addition to the information this provides to those who receive such checks, this is important from a management standpoint so that checks for operating accounts and client trust accounts are not confused with each other. Additionally, proper trust account designation is needed to benefit from FDIC protection.

- "Funds to pay service or other charges or fees imposed by the financial institution, but only in an amount reasonably estimated to be necessary for that purpose" means you may only keep your own funds in the client trust account for this limited purpose, not as a cushion to protect against overdrafts.

- "Funds to pay fees or charges related to credit card transactions or to offset debits for credit card chargebacks, but only in an amount reasonably estimated to be necessary for that purpose" means you may only keep your own funds in the client trust account for this limited purpose, not as a cushion to protect against overdrafts.

- Rule 43(a)(4) directs that funds belonging in part to someone else and in part to you – a settlement check, perhaps, made out to both you and the client – must be deposited into the client trust account. Then you must withdraw the portion belonging to you within a reasonable time, unless the client or third person disputes your right to receive the funds. You must not hold out a portion by noting a cash withdrawal on your deposit slip.

- "... unless the right of the lawyer or law firm to receive it is disputed ..." If a dispute arises about funds in your trust account, you must not withdraw the disputed amount. If you are holding funds that are in dispute, create ticklers to assure that you take action to resolve the dispute as promptly as possible. This is another advantage of reviewing client ledgers monthly – disputed amounts sitting in the trust account will come to your attention each time you do. If the dispute cannot be resolved promptly, you may have an ethical obligation to interplead or file a declaratory action regarding the disputed funds.

<u>What Rule 43(b)(1) says:</u>

Rule 43(b) outlines the nuts and bolts of a client trust account. It's a long, detailed rule, better split into sections.

Standards of Performance.

A. Due professional care must be exercised in the performance of the lawyer's duties under this rule.

B. Employees and others assisting the attorneys in the performance of such duties must be competent and properly trained and supervised.

C. Internal controls within the lawyer's office must be adequate under the circumstances to safeguard funds or other property held in trust.

<u>Some tips about Rule 43(b)(1):</u>

- Lawyers must understand client trust accounting concepts and assure that the staff members they select to assist with trust account maintenance have the necessary knowledge, skills and integrity to adequately protect clients' money. The lawyer must, on an ongoing basis, directly supervise the maintenance of the trust account.

- Safety for client money and other property happens by design. Internal controls need to be revisited periodically; in particular, changes in other office procedures

or staffing levels should be evaluated in terms of any impact they may have on internal control systems. If you have to downsize your office or staff, think about who was and will be performing trust-account-related duties.

- Have all bank statements (not just the trust account statement) go unopened or sent by electronic transmission directly to a designated person, usually the managing partner/shareholder in a firm or the sole practitioner. If the envelope is unsealed, it will be obvious that a violation of this policy has occurred. A lawyer who reviews each month's statement will readily notice discrepancies, such as unusually high or low balances that do not seem in keeping with the transactions with which the lawyer is familiar for that time-period. Other red flags, of course, include returned-item charges and insufficient-funds deposits. The lawyer should also check the canceled checks for any unauthorized signatures.

- From time to time, look through the checks in your checkbook and any unused checks that have not been in your constant sole control. Do this immediately if you suspect an unauthorized person obtained access or, for example, when an employee who had authorized access leaves your employment. Anyone who wants to take checks from your checkbook will probably take them from the middle or the back, where you are less likely to notice right away than if the next sequential numbers are missing.

<u>What Rule 43(b)(2) says:</u>

Trust Account Records.

A. Every active member of the state bar shall maintain, on a current basis, complete records of the handling, maintenance and disposition of all funds, securities and other property belonging in whole or in part to a client or third person in connection with a representation. These records shall include the records required by ER 1.15 and cover the entire time from receipt to the time of final disposition by the lawyer of all such funds, securities and other property. The lawyer shall preserve these records for a period of five years after termination of the representation.

B. A lawyer shall maintain or cause to be maintained an account ledger or the equivalent for each client, person or entity for which funds have been received in trust, showing:

(i) the date, amount and payor of each receipt of funds;

(ii) the date, amount and payee of each disbursement; and

(iii) any unexpended balance.

C. A lawyer shall make or cause to be made a monthly three-way reconciliation of the client ledgers, trust account general ledger/checkbook register, and the trust account bank statement.

D. A lawyer shall retain, in accordance with this rule, all trust account bank statements, cancelled pre-numbered checks (unless recorded on microfilm or stored electronically by a bank or other financial institution that maintains such records for the length of time required by this rule), other evidence of disbursements, duplicate deposit slips or the equivalent (which shall be sufficiently detailed to identify each item), client ledgers, trust account general ledger/checkbook register, and reports to clients.

E. A record shall be maintained showing all property, other than cash, held for clients or third persons in connection with a representation, including the date received, where located and when returned or otherwise distributed.

Some tips about Rule 43(b)(2):

- "Complete records" means all documents related to transactions in the trust account, including but not limited to bank statements, copies of deposit tickets, canceled checks, general ledger/checkbook register, and client ledgers or the equivalent.

- "[S]hall preserve these records for a period of five years after termination of the representation" provides the required time in which records must be kept after final disposition.

- Records must be kept current, not re-created after the fact. You have a responsibility to protect and keep track of any client property, even if it is not money. At any point in time you need to know what property you are holding, when it was received and where it is located.

- Lawyers often forget about retaining duplicate deposit slips. Every deposit that you make into the client trust account should indicate at a minimum from whom the money came. You can do this by making a note of the name on the deposit slip. If the deposit contains money from more than one source, list the names and amounts on the deposit slip. An alternative is to make a copy of the deposited check(s) and attach the copy or copies to the deposit slip. If you are not using a duplicate deposit slip, complete a deposit log or some other documentation to identify the date of deposit, the amount and the corresponding client(s).

- Performing a monthly three-way reconciliation is critical to maintaining your trust account. The totals of each individual client ledger must be added to get a total for

all clients. (Remember to include your "administrative funds" ledger if any funds are held to cover costs of maintaining the account.) The total of the client ledgers should match the balance recorded in the general ledger/checkbook register. If they don't match, investigate immediately. This is very important, as it is not only important that the bank and the lawyer's books agree on the total being held, but also that every penny be accounted for by individual client. If the general ledger/checkbook register total match, the next step is to do a normal reconciliation with the bank statement, making adjustments for outstanding checks (those that have not yet cleared) and deposits in transit (those that were made after the cut-off date for the period covered by the statement).

- Most computerized accounting systems are designed so that the overall totals and the totals broken out by individual client will automatically match. That doesn't mean, however, that an input error couldn't result in money being designated for the wrong client. You still need to review the breakout of funds being held for each client to ensure that all entries were made properly.

- If you're the responsible lawyer and someone else reconciles the account, you still have a responsibility to personally review both the reconciliation report and relevant supporting documentation to ensure that everything has been done properly.

<u>What Rule 43(b)(3) says:</u>

3. *Deposits from Credit Card Transactions*. A lawyer or law firm may permit funds from a credit card transaction to be deposited into a client trust account for payment of advance fees, costs or expenses, and merchant or credit card transaction fees, but only if:
    1. the lawyer has sources of funds, other than client or third-party funds, available at the time of the credit card transaction to replace any funds that may be debited from the account due to a credit card chargeback and any associated fees or charges;

    2. within three business days of receipt of notice or actual knowledge that a chargeback has been made, the lawyer deposits into the trust account his or her own funds in an amount equal to the amount of the chargeback that exceeds the client's credit card funds remaining in the trust account, and any fees or charges associated with the chargeback; and

    3. the trust account contains sufficient funds of the lawyers or law firm at that time of the transaction to pay all merchant and credit card transaction fees, except to the extent that such fees are paid by the client as port of the transaction.

Some tips about Rule 43(b)(3):

a. Permitting the deposit of funds from a credit card transaction into a client trust account for payment of advance fees, costs or expenses, and merchant or credit card transaction fees is at the risk of the lawyer permitting the deposit.

b. If within three business days of receipt of notice or actual knowledge that a chargeback has been made a lawyer uses his or her own funds to replace funds debited from the trust account, as set forth above, the lawyer will not be considered to have committed professional misconduct based upon placement of those credit card funds into the client trust account.

c. If you do not want to take the risk of depositing credit card advanced fees into your trust account, you can ask the client to take a cash advance on the card and pay you in cash.

d. You may also want to think about taking credit card payments for only earned fees.

What Rule 43(b)(4) says:

4. *Disbursement Against Uncollected Funds*. A lawyer generally may not use, endanger, or encumber money held in trust for a client or third person without the permission of the owner given after full disclosure of the circumstances. Except for disbursements based upon any of the four categories of limited-risk uncollected deposits enumerated in paragraph A below, a lawyer may not disburse funds held in trust unless the funds are collected funds. For purposes of this provision, "collected funds" means funds deposited, finally settled by the issuer's bank, and credited without recourse to the lawyer's trust account.

   A. Certain categories of trust account deposits are considered to carry a limited and acceptable risk of failure so that disbursements of trust account funds may be made in reliance on such deposits without disclosure to and permission of clients and third persons owning trust account funds that may be affected by such disbursements. Notwithstanding that a deposit made to the lawyer's trust account has not been finally settled and credited to the account, the lawyer may disburse funds from the trust account in reliance on such deposit under any of the following circumstances, if the lawyer has other sources of funds, other than client or third party funds, available at the time of disbursement to replace any uncollected funds:

      (i) when the deposit is made by certified check or cashier's check;

      (ii) when the deposit is made by a bank check, official check, treasurer's check, money order, or other such instrument where

the payor is a bank, savings and loan association, or credit union;

(iii) when the deposit is made by a check issued by the United States, the State of Arizona, or any agency or political subdivision of the State of Arizona; or

(iv) when the deposit is made by a check or draft issued by an insurance company, title insurance company, or a licensed title insurance agency authorized to do business in the state of Arizona.

In any of the above circumstances, a lawyer's disbursement of funds from a trust account in reliance on deposits that are not yet collected funds is at the risk of the lawyer making the disbursement. If any of the deposits fail, for any reason, the lawyer, upon obtaining knowledge of the failure, must immediately act to protect the property of the lawyer's clients and third persons. If the lawyer accepting any such check personally pays the amount of any failed deposit within three business days of receipt of notice that the deposit has failed, the lawyer will not be considered guilty of professional misconduct based upon the disbursement of uncollected funds.

B. A lawyer's disbursement of funds from a trust account in reliance on deposits that are not yet collected funds in any circumstances other than those four categories set forth above, when it results in funds of clients or third persons being used, endangered, or encumbered, will be grounds for a finding of professional misconduct.

<u>Some tips about Rule 43(b)(4):</u>

- Normally you must wait until a deposit clears the issuing bank before disbursing against it.
    - It may take days or weeks after you make a deposit before the money becomes "collected funds." A client's funds aren't available for you to use on the client's behalf until they have cleared the banking process and been credited by the bank to your client trust account. If you write a check for a client at any time before that client's funds clear the banking process and are credited to your client trust account, either the check will bounce, or you will be using other clients' money to cover the check.
    - Every bank has different procedures, so when you open your client trust account, get the bank's schedule of when funds are available for

withdrawal. Even if you make a cash deposit, the money may not be available for use until the following business day. If you deposit a personal check from an out-of-state bank, the money will take longer to become available. Either way, until the bank has credited a client's deposit to your client trust account, you cannot pay out that money for the client.

- You also need to know what your bank's cut-off time is for transactions to be posted on that same business day. If your bank's cut-off time is 1:00 p.m., any deposits that you make after 1:00 p.m. will be posted on the next business day, even if the bank is open until 5:00 p.m. For example, your client arrives at 3:30 p.m. and gives you $5,000 in cash, which you immediately deposit. At 4:00 p.m., you write a client trust account check to an investigator against that money. If the investigator presents the check for payment at the bank before it closes at 5:00 p.m., the check will either bounce or be covered by other clients' money.

- The fact that a deposit may be immediately credited to your account is irrelevant. If you deposit a check and your bank immediately credits your account, then disburse against that deposit, you will have problems if the check fails to clear the issuing bank. Your bank will, of course, deduct the amount of the returned item from your account. If you have disbursed against that now-returned item, other clients' funds are being used when the amount is deducted from your account.

- You also cannot accept an arrangement for overdraft protection for a trust account. Rule 43(a) If the bank deposits funds from any source, such as a transfer from your savings account, a credit line or a credit card to make up deficiencies in the account, you are introducing to the account funds that do not fall into one of the categories of funds appropriately deposited to a trust account and are commingling your funds with that of your clients.

- Although you normally must wait until a deposit clears the issuing bank to disburse against it, in some limited circumstances you may disburse against it before then.

    - Only the four categories of instruments qualify as limited-risk deposits:

        (i) when the deposit is made by certified check or cashier's check;

(ii) when the deposit is made by a bank check, official check, treasurer's check, money order, or other such instrument where the payor is a bank, savings and loan association, or credit union;

(iii) when the deposit is made by a check issued by the United States, the State of Arizona, or any agency or political subdivision of the State of Arizona; or

(iv) when the deposit is made by a check or draft issued by an insurance company, title insurance company, or a licensed title insurance agency authorized to do business in the state of Arizona.

- You may only disburse against one of these limited-risk uncollected deposits if you have personal funds available to cover the deposit in the event the deposit is returned or fails for any reason. This may not be a problem for small checks, but what about if the $50,000 insurance check fails for any reason? Do you have personal funds – *available to cover the check within three business days* – to cover it?

- Disbursing funds in reliance on deposits not yet collected – other than those limited-risk deposits -- is at your risk, as doing so may result in funds of clients or third persons being used, endangered, or encumbered.

<u>What Rule 43(b)(5) says:</u>

> *Methods of Disbursement*. All trust account disbursements shall be made by pre-numbered check or by electronic transfer, provided the lawyer maintains a record of such disbursements in accordance with the requirements of this rule. <u>All instruments of disbursement shall be identified as a disbursement from a trust account.</u>

<u>Some tips about Rule 43(b)(5):</u>

- You may disburse out of your client trust account only by pre-printed, pre-numbered check or by electronic transfer that generates a record of the transaction. This means you may not transfer funds out of your client trust account by withdrawing money using an ATM card, by using a withdrawal ticket to remove funds at the teller window, or by receiving cash back from a deposit.

- If you just opened a client trust account, you may not use the "temporary" checks your bank may provide to you. Because of this, you need to think

ahead. You must open an account in adequate time to obtain pre-numbered checks *before* you need to disburse money from the account, or to make sure the disbursement is made electronically and that you have a corresponding record of the transfer.

- Regardless of which method you use to disburse from the trust account, it must be identified as a trust account disbursement.

What Rule 43(c) says:

Certificate of compliance. Every active member of the state bar shall on or before February 1 of each year file with the board a certificate certifying compliance with the provisions of this rule and ER 1.15 of the Arizona Rules of Professional Conduct, or that he or she is exempt from the provisions of this rule and ER 1.15. The certificate of compliance shall state as follows:

> Annual Certificate of Compliance
>
> I have read Rule 43, Rules of the Supreme Court, and ER 1.15, Arizona Rules of Professional Conduct, and certify that I am in compliance with the provisions thereof, or am exempt from such provisions as therein provided.
>
> Dated: _____
>
> Signature: _____
>
> Type or print name: _____
>
> As an alternative to filing a written certificate, the board may allow certification to be filed electronically in a method and form as approved by the board.

A tip about Rule 43(c):

Make sure that you read Rule 43 and ER 1.15 each and every time you sign the certification. The rules may have changed since the last time you signed the certification.

What Rule 43(d) says:

Account Examination; Random Examination.

1. *Authority.* The state bar shall evaluate all information coming to its attention by

charge or otherwise indicating a possible violation of the trust account rules, and such information shall be treated and processed as is any other charge against a lawyer. In addition to trust account examinations that shall be conducted based upon information coming to the bar's attention, the state bar may also conduct random trust account examinations of any member's trust account(s), in accordance with Guidelines developed by the Board of Governors and approved by the Supreme Court.

2. *Scope of Examination.* The state bar may verify all funds, securities and other property held in trust by the member, and all related accounts, safe deposit boxes, and any other form of maintaining trust funds, securities or property, together with deposit slips, cancelled checks, and all other records pertaining to transactions concerning trust funds, securities and property.

3. *Rebuttable Presumption.* If a lawyer fails to maintain trust account records required by this rule or ER 1.15, or fails to provide trust account records to the state bar upon request or as ordered by a panelist, a hearing officer, the commission or the court, there is a rebuttable presumption that the lawyer failed to properly safeguard client or third person's funds or property, as required by this rule and ER 1.15.

4. *Limited Exception for Out-of-State Members.* All funds, securities and other property of clients and third persons held by an Arizona-licensed lawyer whose law office is situated in another state shall not be subject to investigation, examination or verification except to the extent such funds and property are related to matters affecting Arizona clients.

5. *Trust Account Examination and Verification Expenses.* A member whose trust account has been examined or verified pursuant to this rule shall not be responsible for the costs and expenses related to the examination or verification, unless such costs and expenses are imposed pursuant to an order of diversion as set forth in Rule 56(a) or in conjunction with imposition of a disciplinary sanction as set forth in Rule 55(c) or Rule 60(b).

<u>Some points of note and tips about Rule 43(d):</u>

- The State Bar investigates non-sufficient fund notices it receives from banks that participate in the IOLTA program.

- In addition, the State Bar may now conduct random trust account examinations. As of December 2009, however, the Board of Governors had not developed guidelines. Until the guidelines have been established, no random trust account examinations will be performed.

- It is now the lawyer's responsibility to prove he or she has safeguarded client funds

if the lawyer does not keep appropriate records.

- A lawyer is only responsible for the cost of a trust account examination if the investigation results in diversion or some type of disciplinary sanction.

What Rule 43(e) says:

> **Confidentiality.** The provisions of Rule 70(b) of these rules shall apply to records acquired during examinations conducted pursuant to this rule. In those instances where the state bar conducts a random examination of a member's trust account(s) that does not result in a disciplinary charge, all information received as a result of that examination shall be kept strictly confidential and shall not be released to any person(s).

A tip about Rule 43(e):

Make sure you keep your original records, as the records given to the state bar may be destroyed after the examination.

What Rule 43(f) says:

Establishment of Trust Accounts; State Bar Oversight.

1. A lawyer or law firm receiving funds belonging in whole or in part to a client or third person in connection with a representation must hold the funds in one of the following types of accounts:

- a pooled interest-bearing or dividend-earning trust account ("IOLTA account") on which the interest or dividends accrue for the benefit of the Arizona Foundation for Legal Services and Education ("Foundation");

- a separate interest-bearing or dividend-earning trust account for the particular client or client's matter on which the interest or dividends, net of any reasonable service or other charges or fees imposed by the financial institution or investment company in connection with the account, will be paid to the client; or

- a pooled interest-bearing or dividend-earning trust account, with subaccounting provided by the lawyer or the law firm, which will provide for computation of interest or dividends earned by each client's funds and the payment thereof, net of any reasonable service or other charges or fees imposed by the financial institution or investment company in connection with the account, to the client.

2. In determining which type of account provided for in section (f)(1) to use, a lawyer or law firm shall take into consideration the following factors:

A. the amount of funds to be deposited;

B. the expected duration of the deposit, including the likelihood of delay in the matter for which the funds are held;

C. the rates of interest or yield at financial institutions where the funds are to be deposited;

D. the cost of establishing and administering a separate non-IOLTA account for the client's benefit, including service charges, the costs of the lawyer's services, and the costs of preparing any tax reports required for income accruing to the client's benefit;

E. the capability of financial institutions to calculate and pay income to individual clients; and

F. any other circumstances that affect the ability of the client's funds to earn a net return for the client.

Funds should be deposited in an IOLTA account as provided for in section (f)(1)(A) if the interest does not cover the cost of opening and maintaining a separate interest-bearing or dividend-earning account. The State Bar shall not pursue a disciplinary matter against any lawyer or law firm solely based on the good-faith determination of the appropriate account in which to deposit or invest client funds.

3. A lawyer or law firm must maintain any client trust account provided for in section (f)(1) only at a regulated financial institution, which is either (i) a financial institution authorized by federal or state law to take deposits and conduct financial transactions with Arizona lawyers and is insured by the Federal Deposit Insurance Corporation or any successor insurance corporation(s) established by federal or state laws or (ii) any open-ended investment company registered with the Securities and Exchange Commission that is authorized by federal or state law to take deposits and conduct financial transactions with Arizona lawyers. A regulated financial institution must agree to comply with the requirements of section (f)(4) below and agree to pay IOLTA interest to the Foundation. The lawyer or law firm must ensure that:

A. withdrawals or transfers can be made on demand, subject only to any notice period which the institution is required to reserve by law or regulation, and

B. the deposited funds are invested in the higher earning return of:

i. an interest-bearing checking account;

ii. a money-market deposit account with or tied to checking;

iii. a sweep account, which is a money-market fund or daily (overnight) financial institution repurchase agreement invested solely in or fully collateralized by U.S. Government Securities; or

iv. an open-end money-market fund solely invested in or fully collateralized by U.S. Government Securities.

A daily financial institution repurchase agreement may be established only with a regulated institution that is "well capitalized" or "adequately capitalized" as those terms are defined by applicable federal statutes and regulations. An open-end money market fund must be invested solely in U.S. Government Securities or repurchase agreements fully collateralized by U.S. Government Securities, must hold itself out as a "money-market fund" as that term is defined by federal statutes and regulations under the Investment Company Act of 1940, and at the time of the investment must have total assets of at least $250,000,000. "U.S. Government Securities" refers to U.S. Treasury obligations and obligations issued or guaranteed as to principal and interest by the United States or any agency or instrumentality thereof.

C. All service charges to the account are reasonable, related to the cost of maintaining the account, and computed in accordance with the financial institution's standard accounting practices.

D. The financial institution sends notification immediately to the State Bar chief bar counsel of any properly payable instrument that is presented for payment against a client trust account containing insufficient funds, uncollectible funds, or a negative available balance, regardless of whether the financial institution honors the instrument. All occurrences shall be reported to the State Bar regardless of the cause.

If a financial institution ceases to operate as a regulated financial institution and has no successor operating as a regulated financial institution, a lawyer or law firm that maintains an account listed under section (f)(1) at that financial institution must, upon receiving notice of the financial institution's change in status, promptly notify any clients whose funds may be affected by the change in status, promptly transfer, to the extent possible, any client trust account funds from that financial institution into another account provided for in section (f)(1), and promptly deposit into the other account provided for in section (f)(1) any insurance, collateral, or proceeds resulting from the financial institution's change in status.

4. In addition to the requirements of section (f)(3), a lawyer or law firm may only maintain an IOLTA account as provided for in section (f)(1)(A) at an authorized regulated financial institution. To be designated as authorized, a regulated financial institution must sign a participation certification before the fiscal year beginning July 1, with the State Bar

as representative of its members, and the Foundation as a third-party beneficiary and administrator of the interest or dividends.

A. The participation certification must:

i. define a reasonable charge for managing IOLTA accounts, which may include fees for reporting and recordkeeping;

ii. direct that interest or dividends, net of any reasonable service charges or fees, be remitted at least quarterly to the Foundation;

iii. provide that the financial institution transmit, with each remittance to the Foundation, a statement, as directed by the Foundation, showing information including the name of the lawyer or law firm on whose account the remittance is sent, the period for the remittance submitted, the account number, the account status, the rate of interest applied or the dividends earned, and the charges imposed against the interest remitted;

iv. provide that the financial institution transmit a report on each separate account, similar to the report required by section (f)(4)(a)(iii), to the lawyer or law firm opening said trust account;

v. direct that if the financial institution receives a subpoena duces tecum requesting documents pertaining to a lawyer's IOLTA account with the financial institution, the financial institution shall provide the documents specified in the subpoena duces tecum;

vi. provide that the terms apply to all branches of the regulated financial institution holding Arizona IOLTA accounts;

vii. provide that the financial institution be allowed to charge a particular lawyer or law firm for the reasonable cost of producing the reports and records required by this rule;

viii. provide that the participation certification may not be cancelled by the regulated financial institution except upon 30 days' advance written notice to the State Bar and the Foundation;

ix. provide that the participation certification may not be cancelled or revoked except upon 30 days' advance written notice to the regulated financial institution;

x. provide for an annual approval period; and

xi. provide that any participation certification continues in existence during any time the authorized regulated financial institution is attempting to become reauthorized.

B. If an authorized regulated financial institution does not sign the participation certification for the fiscal year beginning July 1 during which the regulated financial institution wishes to be re-authorized:

i. The matter will be referred to a mediator selected by the Court.

ii. The mediator will have 60 days to meet with the parties and attempt to reach a settlement.

iii. If after 60 days with mediation the parties do not reach a participation certification as provided for in section (f)(4)(A) above, the State Bar shall:

(a) notify the Supreme Court that the financial institution has failed to sign a participation certification for the following fiscal year;

(b) notify members who maintain trust accounts at that regulated financial institution that the regulated financial institution has failed to sign a participation certification for the following fiscal year; and

(c) notify other members that the regulated financial institution is not in compliance and that no new trust accounts may be opened at that financial institution for the following fiscal year.

iv. Upon receiving the State Bar's request provided for in section (f)(4)(B)(iii)(a), the Court may issue an order de-authorizing a previously authorized regulated financial institution that is seeking to become reauthorized.

C. The State Bar and the Foundation shall ensure the maintenance of a website listing of authorized regulated financial institutions' status.

5. If the State Bar and the Foundation become aware of information indicating that an authorized regulated financial institution has not complied with the duties provided for in section (f), the State Bar shall notify the regulated financial institution of its failure to comply and that it has 90 days to cure its noncompliance.

A. If, after 45 days, the noncompliance has not been cured, then the State Bar shall:

i. notify members who maintain trust accounts at that regulated financial institution that the regulated financial institution had been given 90 days to cure its noncompliance and to date it has not complied;

ii. notify other members that the regulated financial institution is not in compliance and that no new trust accounts may be opened at that financial institution;

iii. notify the Supreme Court that the financial institution is in noncompliance and had been given 90 days to cure its noncompliance.

B. If the financial institution cures its noncompliance, the State Bar shall promptly notify its members and the Supreme Court.

C. If the financial institution fails to cure the noncompliance, the State Bar shall file with the Court a request for termination of authorized status of that financial institution.

D. The Court may issue an order terminating the authorized status of the financial institution and instructing the State Bar to:

i. assure removal of the institution from the list of authorized financial institutions, and

ii. notify all members of the removal.

E. Upon receiving the notice provided for in section (f)(5)(D):

i. Members who maintain trust accounts at the de-authorized financial institution shall:

(a) have 90 days to transfer their accounts to an authorized financial institution, and
(b) by the end of 90 days, notify the State Bar that their trust accounts have been transferred and provide pertinent account information.

ii. Members who continue to maintain trust accounts at the de-authorized financial institution more than 90 days after notice or who fail to tell the State Bar that they have done so shall be referred to the State Bar Lawyer Regulation Office.

6. Interest or dividends generated on accounts specified in section (f)(1)(A) shall be paid by the financial institution or investment company to the Foundation. The Foundation shall use the interest or dividends solely to:

A. support programs designed to assist in the delivery of legal services to the poor and law-related education programs designed to teach young people, educators and other adults about the law, the legal process and the legal system;

B. fund studies or programs designed to improve the administration of justice;

C. maintain a reasonable reserve; and

- pay the actual costs of administering this rule and the activities set forth above.

7. In addition to other obligations under section (f) of this rule, all lawyers admitted to practice in this state shall:

A. as a condition thereof, consent to the reporting and production requirements set forth in this rule, and

B. provide information requested by the State Bar on the annual dues statement regarding any and all client trust accounts they maintain.

Some tips about Rule 43(f):

- If a lawyer receives a large enough sum of client money to generate interest for the client above the charges of establishing and maintaining an account, or a smaller sum that will be held for a long period of time, it may be appropriate to establish a separate interest-bearing or dividend-earning account on behalf of the client. You will need the client's taxpayer identification or social security number to do this. Be sure your client is aware that he or she will not only receive the interest or dividends, but will be responsible for any taxes on the interest or dividends.

- If you choose to use subaccounting to pay interest to individual clients from a pooled account, you may do so.

- See section IV for information regarding FDIC coverage on trust accounts.

- Use only an approved financial institution for your trust account.

- Approved financial institutions must report insufficient funds checks to the State Bar, which then will conduct an investigation. Even if the NSF check resulted from a mistake, you will need to be prepared to respond to the State Bar's investigation.

- A list of approved financial institutions can be found on the Arizona Foundation for Legal Services & Education website.
  http://www.azflse.org/azflse/IOLTA/allbanks.cfm

(g) Reserved.

What Rule 43(h) and (i) say:

(h) Suspension of Member. Any active member who fails to comply with requirements of this rule shall be suspended summarily by order of the board upon notice by the state bar pursuant to Rule 62(a)(4), provided that a notice by certified, return receipt mail of such non-compliance shall have been sent to the member, mailed to the member's last address of record in the state bar office at least thirty days prior to such suspension.

(i) Reinstatement of Member. A lawyer who has been suspended for failure to comply with this rule may be reinstated by compliance with those provisions and notice to the board by the state bar of such compliance.

Some tips about Rule 43(h) and (i):

- You may be summarily suspended if you fail to comply with Rule 43. If the State Bar knows that a lawyer is not complying with the trust account rules, it may notify the Board of Governors of the lawyer's failure to comply with Rule 43. Thirty days thereafter, and after proper notice to the lawyer, the Board may order the lawyer's suspension.

What Rule 43(j) says:

(j) Applicability of Rule. Every lawyer admitted to practice law in Arizona shall comply with the provisions of this rule regarding funds received, disbursed or held in Arizona, and funds received, disbursed or held on behalf of an Arizona client or a third person in connection with the representation of an Arizona client.

A tip about Rule 43(j):

If you practice in multiple states, you may have to comply with more than one set of trust account rules. Rule 43(j) applies even if you practice out of state but handle Arizona matters for Arizona clients. How you comply with Arizona rules could impact your ability to comply with the rules of other states in which you may be admitted.

SECTION III: KEY CONCEPTS IN CLIENT TRUST ACCOUNTING

Seven key concepts are all you need to understand your client trust accounting responsibilities.

A. Separate Clients Are Separate Accounts

Client A's money has nothing to do with Client B's money. Even when you keep them in a common client trust account, each client's funds are completely separate from those of all your other clients. In other words, you may NEVER use one client's money to pay either another client's or your own obligations.

The most direct way to keep one client's money separate from another's would be to create individual bank accounts for each client. But in most private law practices, this is impractical. Most lawyers keep many clients' money in one pooled client trust account. This is the pooled trust account authorized by Rule 43 and known commonly – albeit redundantly -- as an "IOLTA (Interest on Lawyers Trust Account) account."

When you keep your clients' money in an IOLTA account, you distinguish one client's money from another's by keeping a client ledger of each individual client's funds. The client ledger tells you how much money you've received on behalf of each client, how much money you've paid out on behalf of each client, and how much money each client has left in your IOLTA account. If you are holding money in your IOLTA account for 10 clients, you have to maintain 10 separate client ledgers. If you keep each client's ledger properly, you will always know exactly how much of the money in your IOLTA account belongs to each client. If you don't, you will lose track of how much money each client has, and when you make payments out of your IOLTA account, you won't know which client's money you are using.

B. You Can't Spend What You Don't Have

Each client has only his or her own funds available to cover costs and expenses, no matter how much money belonging to other clients is in your IOLTA account. Your account might have a balance of $100,000, but if you are only holding $10 for a client, you can't write a check for $10.50 on behalf of that client without using some other client's money.

The following example graphically illustrates this concept. Assume you are holding a total of $5,000 for four clients in your IOLTA account as follows:

Client A	$1,000
Client B	$2,000
Client C	$1,500
Client D	$500
Total	**$5,000**

If you write a check for $1,500 for Client D, $1,000 of that check is going to be paid for by Clients A, B and C. The funds you are holding in trust for them are being used for Client D's expenses. You should have a total of $4,500 for Clients A, B and C, but you only have $3,500 left in the trust account. In State Bar disciplinary matters, a finding of a failure to maintain a sufficient client trust account balance will support a finding of misappropriation.

C. There's No Such Thing As a Negative Balance

Even though improper, it's not uncommon for people to write personal checks on an account that either doesn't have sufficient funds or against money they haven't deposited yet or money deposited that is uncollected (not cleared yet). If a person writes a check against an account in such a situation, the result is a negative balance. In client trust accounting, there's no such thing as a negative balance. A negative balance is at best a sign of negligence and, at worst, a sign of theft. A lawyer may **NEVER** have a negative balance either on an individual client ledger or in the IOLTA account.

In client trust accounting, there are only four possibilities:

- You have a positive balance (while you are holding money for a client);
- You have a **zero** balance (when all the client's money has been paid out);
- You have a small amount of money in your account to cover bank service costs but no client funds; or
- You have a balance of less **than zero** (a so-called "negative balance") and a problem.

D. Timing Is Everything

It takes from a day to several weeks after you make a deposit before the money becomes available for use. A client's funds aren't "available" for you to use on the client's behalf until they have cleared the banking process and been credited by the bank to your client trust account. (This is especially true when you receive an insurance company's settlement draft, which cannot clear until the company actually receives the draft at its home office during the bank collection process and honors the draft. Thus, insurance company settlement drafts will take longer to clear your account.) If you write a check for a client at any time *before* that client's funds clear the banking process and are credited to your client trust account, ordinarily either the check will bounce or you will be using other clients' money to cover the check.

The time it takes for client trust account funds to become available after deposit depends on the form in which you deposit them. Every bank has different procedures, so when you

open your IOLTA account, get the bank's schedule of when funds are available for withdrawal. Depending on the instrument, you may have to wait as many as 15 working days before you can be reasonably confident that the funds are available. For example, even if you make a cash deposit, the money may not be available for use until the following day. If you deposit a personal check from an out-of-state bank, the money will take longer to be available. Either way, until the bank has credited a client's deposit to your client trust account, you can't pay out any portion of that money for that client.

Rule 43(b)(4), however, allows a lawyer to disburse against certain types of checks without waiting for those deposits to be finally settled and credited to the IOLTA account. But a lawyer takes a risk by relying on these limited-risk deposits. Rule 43(b)(4)(A) requires that the lawyer doing so must have personal funds sufficient to cover the limited-risk deposit in the event the deposit fails. Allowable limited-risk deposits include government and insurance company checks.

You also need to know what time your bank has set as the deadline or cut-off for posting deposits to that day's business and for paying checks presented to it. Otherwise, even when you have deposited cash, you may end up drawing on uncollected funds. If your bank's cut-off time is 1:00 p.m., any deposits that you make after 1:00 p.m. will be posted on the next business day, even if the bank is open until 5:00 p.m. For example, your client arrives at 3:30 p.m. and gives you $5,000 in cash, which you immediately deposit. At 4:00 p.m., you write a client trust account check to an investigator against that money. If the investigator presents the check for payment at the bank before it closes at 5:00 p.m., the check will either bounce or be covered by other clients' money.

You may be tempted to do your client a favor by writing a check to the client for settlement proceeds before the settlement check has cleared because you know there's money belonging to other clients in your client trust account to cover this client's check. Depending on the circumstances, your client may insist that you do this. Don't. If you do, you'll end up writing a check to one client using other clients' money. You shouldn't help one client at the expense of your obligations to your other clients. In other words, no matter how expedient or kind or convenient it seems, don't make payments on your clients' behalf before their deposited funds have cleared. Otherwise, sooner or later, you'll end up spending money your clients don't have.

Some banks offer an arrangement in which the bank agrees to immediately credit accounts for deposits while the bank waits for the funds from another financial institution. This, in essence, is a loan to the lawyer that is deposited in the client trust account, and thus a commingling of funds. An "instant credit" arrangement may also be offered as a form of overdraft protection. Again, this results in commingling of funds and is not allowed.

E. You Can't Play the Game Unless You Know the Score

In client trust accounting, there are two kinds of balances: the "running balance" of the money you are holding for each *client* and the "running balance" of each *client trust*

account.

A "running balance" is the amount you have in an account after you add in all the deposits (including interest earned, for example) and subtract all the money paid out (including bank charges for items such as wire transfers.). In other words, the running balance is what's in the account at any given time. The running balance for each *client* is kept on the client ledger, and the running balance for each *client trust account* is kept on the general ledger/checkbook register.

Maintaining a running balance for a client is simple. Every time you make a deposit on behalf of a client, you write the amount of the deposit in the client ledger and *add* it to the previous balance. Every time you make a payment on behalf of the client, you write the amount in the client ledger and *subtract* it from the previous balance. The result is the running balance. That's how much money the client has left to spend.

You figure out the running balance for the client trust account the same way. Every time you make a deposit to the client trust account, you write the amount of the deposit in the general ledger and *add* it to the previous balance. Every time you make a payment from the client trust account, you write the amount in the general ledger/checkbook register and *subtract* it from the previous balance. The result is the running balance. That's how much money is in the account.

Since you can't spend what you don't have, you should check the running balance in each client's client ledger before you write any client trust account checks for that client. That way, if your records are accurate and up-to-date, it's almost impossible to pay out more money than the client has in the account.

F. The Final Score Is Always Zero

The goal in client trust accounting is to make sure that every dollar you receive on behalf of a client is ultimately paid out. What comes in for each client must equal what goes out for that client; no more, no less.

Many lawyers have small, inactive balances in their client trust accounts. Sometimes these balances are the result of a mathematical error, sometimes they are part of a fee you forgot to take, and sometimes a check you wrote never cleared or wasn't cashed.
Whatever the reason, as long as the money is in your client trust account, you are responsible for it. The longer these funds stay in the bank, the harder it is to account for them. Therefore, you should take care of those small, inactive balances as soon as possible, including, if necessary, following up with payees to find out why a check hasn't cleared.
If you cannot locate the owner of client trust account funds you are holding or if you are unable to determine the ownership, you should consult Ariz. *Ethics Op.* 97-03 for guidance or seek ethics advice from private counsel or from the State Bar's ethics hotline. Ethics opinions since 1985 are available by searchable format on the State Bar's website,

www.azbar.org. The ethics hotline is 602-340-7284.

G. Always Maintain an Audit Trail

An "audit trail" is the series of bank-created records, such as canceled checks and bank statements that make it possible to trace what happened to the money you handled. An audit trail should start whenever you receive funds on behalf of a client and should continue through the final check you issue against them. Without an audit trail, you have no way to show that you have taken proper care of your clients' money, or to explain what you did with the money if any questions come up. The audit trail is also an important tool for tracking down accounting errors. If you don't maintain an audit trail, you will find it hard to correct the small mistakes, like errors in addition or subtraction, and the big mistakes, like miscredited deposits, that are inevitable when you handle money.

The key to making a good audit trail is being descriptive. Let's say you are filling out a deposit slip for five checks relating to three separate clients. All the bank requires you to do is write in the bank identification code for each check and the check amounts. This doesn't identify which client the money belongs to. If you include the name of the client and keep a copy or make a duplicate, you will know which client the check was for, which is the purpose of an audit trail. That will make it easy to answer any questions that come up, even years later.

By the same token, every check you write from your client trust account should indicate which client it's being written for, so that it's easy to match up the money with the client. That means you should NEVER make out a client trust account check to cash, because there's no way to know later who actually cashed the check. If you are handling more than one case for the client, indicate which matter the payments and receipts relate to on your checks and deposit slips.

A good audit trail, one that will make it easy for you to explain what happened to each client's money and to correct accounting errors, should include the following:

- The initial *deposit slip* (or a duplicate copy or bank receipt). This should show the date the deposit slip was filled out; the amount of the deposit; the name or file number of the client on whose behalf the money was received; whom the money came from; and the bank's date stamp showing the date the deposit was actually received.

- *The bank statement* that shows when the deposit was actually posted by the bank.
- *The checkbook stub*, which should show when payments were made, how much the payments were, to whom they were made and in connection with which client matter they were made.

- *The canceled check or canceled-check image*. In a good audit trail, the check

should show the date the check was drawn; the amount of payment; to whom the check was made out; the purpose of the check (or the matter it relates to); the order in which the check was negotiated (from the endorsements); and the date it was deposited for collection.

- The bank statement that shows the date the trust account was actually charged for the check.

- Copies of the front and back of any executed drafts, especially insurance settlement drafts, received on behalf of a client.

SECTION IV: OPENING A CLIENT TRUST ACCOUNT

You need to establish your client trust account using the taxpayer identification number of the Arizona Foundation for Legal Services and Education (AZFLSE), not your firm's taxpayer identification number or your social security number. Most banks are familiar with establishing client trust accounts.

The Arizona Foundation for Legal Services & Education Taxpayer ID Number is 95-3351710.

You may obtain from the State Bar of Arizona (call the Trust Account Hotline at 602-340-7305) an IOLTA Enrollment Form and a Notice to Financial Institution. The information is also available on the AZFLSE website:

http://www.azflse.org/azflse/IOLTA/lawyersenroll.cfm

In other words, whenever you receive or hold money for clients – or any other persons with whom you have a fiduciary relationship that is related to the representation of a client – you have to deposit the money into a specifically labeled client trust account. As detailed below, client trust accounts are a special kind of bank account. Bankers who have experience with them can help you set up and administer your client trust account properly. When you first open the account, make sure the bankers you're dealing with know what a client trust account is; if they don't, ask to work with someone who does.

A. General Do's and Don'ts

Client trust accounts:

Must, per Rule 43(f)(3), Ariz. R. Sup. Ct., be "at a regulated financial institution on which withdrawals or transfers can be made on demand, subject only to any notice period which the institution is required to reserve by law or regulation and, at the direction of the lawyer, invested to the extent practicable in the higher earning return of either (i.) an interest-bearing checking account; (ii.) a money-market deposit account with or tied to checking; (iii.) a sweep account, which is a money-market fund or daily (overnight) financial institution repurchase agreement invested solely in or fully collateralized by U.S. Government Securities; or (iv.) an open-end money-market fund solely invested in or fully collateralized by U.S. Government Securities. (This section of Rule 43 explains in detail the specific regulations regarding such investments).

Should be maintained in a financially stable bank. This isn't a rule; it's common sense. As your clients' fiduciary, you're in for some trouble if the bank you've put their money in goes under. Even if your bank is federally insured, that insurance only covers $250,000 per client. (The per-client limit includes *all* money the client has on deposit at that bank. In other words, if you are holding $180,000 for a client at a certain bank, and the client has

another $140,000 on deposit at the same bank, only $250,000 of the $320,000 the client is holding in the bank is covered.) Even if all your clients' money is covered, by the time the FDIC pays your clients their money, your clients could have, for example, missed a business opportunity. (As we will discuss later, if your bank goes under, you also may have a hard time getting copies of your client trust account records.) Like most client trust accounting problems, the answer to this is simple; keep your client trust accounts in banks that you're reasonably sure are financially secure. Lawyers should monitor FDIC coverage continuously to keep up with the changes in coverage. http://www.fdic.gov

Must be identified as an "IOLTA Account," "client trust account" or similar designation. Whatever name you choose, you can avoid all kinds of problems if the name of the account is prominently displayed on all your client trust account checks, deposit slips and other documents. Make sure that papers relating to your client trust account look different from those relating to your personal account or your general office account. For example, you can have your client trust account checks printed on paper that's a different color than your other checks.

Should limit accessibility of funds. Ideally, you should be the *only* person authorized to sign client trust account checks and otherwise pay out client funds. However, for practical reasons, many practitioners make their secretaries, bookkeepers or spouses authorized signatories. Since *you* are individually and personally accountable for all client funds you receive or hold in trust, and since this accountability can't be delegated to anyone else, allowing other people access to your client trust account is risky. By the same token, you should never pre-sign blank client trust account checks and leave them for employees to issue, or use a signature stamp.

Must NOT have ATM access. Your fiduciary responsibility is to account for your clients' money. When you write a client trust account check, you create an audit trail that makes it easy to trace who the money came from and where it went. A client trust account with ATM access makes it possible for you—or anyone who knows the account code—to withdraw your clients' money in cash, and it's very hard to account for cash. ATM withdrawals are an audit trail disaster. When you make an ATM withdrawal, the only record of what happened to the money is a little slip of paper that shows the date and the amount of the withdrawal; there's nothing that shows which client's money was withdrawn, who withdrew the money or who the money was paid to. This includes withdrawing your fees, since there's no indication of which client's fees you were paying. Even if you put all the descriptive information on an ATM receipt, it won't show to your clients or a State Bar investigator what happened to the money.

Must NOT include automatic overdraft protection. Generally, automatic overdraft protection means that whenever you write a check for more money than is in your account, the bank will automatically make you a personal loan and apply those funds to your account to keep the check from bouncing. This optional account feature may also be offered as an "instant credit" arrangement where the bank agrees to immediately credit accounts for deposits while the bank waits for the funds from another financial institution.

Overdraft protection that automatically deposits a set amount (i.e., a deposit or credit of $200 to cover a $155 overdraft) will leave a residual balance of funds after covering the amount of insufficient funds. This residue in your client trust account is money that belongs to you and not to any of your clients and creates a commingling problem.

By the time you hear from the State Bar, several weeks may have passed since you had the problem with your client trust account. When an overdraft of a client trust account occurs, it is possible that your bank made an error or is aware of funds not yet credited to your account. The bank may owe you as their customer, an explanation, but it is your responsibility to provide an explanation to the State Bar.

B. IOLTA Accounts

A lawyer or law firm receiving client funds shall maintain a pooled interest bearing or dividend earning trust account for deposit of client funds, unless the funds are expected to earn net income for the client in excess of the costs incurred to secure such income. The interest the account earns will be paid to the AZFLSE. Rule 43(f)(2), Ariz. R. Sup. Ct.

Because most attorneys at some time hold a client's money that is nominal or will be held for a short period of time, the chances are that you will need to set up a common client trust account, which for convenience we've referred to as an IOLTA account. Although not as common, the rules do allow for a separate interest bearing trust account for a particular client or a pooled interest bearing account with sub-accounting provided by the lawyer or law firm. *See* Rule 43(f)(3)(A) and (B), Ariz. R. Sup. Ct.

The idea behind the AZFLSE is that lawyers often hold amounts of money for clients that are so small or will be held for such short periods of time that the interest the money could earn for the client if it were held in a separate interest-bearing account would be less than the costs involved in earning or accounting for the interest. However, when these amounts of money are held in a common client trust account, they collectively can generate substantial interest. The AZFLSE requires that this aggregate interest, which would otherwise benefit only the bank, be used to fund programs to assist delivery of legal services to the poor, to support law related education, to fund studies and programs, and to improve the administration of justice.

C. Know Your Bank

From the moment you make the first deposit into your client trust account, handling your clients' money means dealing with your bank. Every bank has different procedures; not knowing those procedures can hurt you and your clients. For every bank in which you maintain a client trust account, make sure you get the answers to the questions in Section III (D) (Timing is Everything) your bank's schedule for clearing deposits, your bank's daily deadline for crediting deposits and your bank's daily deadline for paying checks drawn on it—and the following:

• On what day of the month does the bank usually send out statements of account activity? Every bank sends out monthly statements that show what deposits have been credited to and what payments have been withdrawn from each account. Rule 43(b)(2)(C) requires you to do monthly three-way reconciliations of your client trust accounts to make sure that your records match the bank's records. If you know when you can expect to receive the bank statement, you can schedule a regular time every month to do this.

• Knowing when to expect your bank statement can also help you guard against theft by an associate or an employee. If someone is stealing from your client trust account, the bank statement should show it. An in-house thief may try to hide by concealing incriminating bank statements; if you're looking for the bank statement in the mail every month, the thief won't be able to hide for long. Be sure to review both the bank statements and canceled checks to avoid potential problems.

• What does your bank charge for and how much will you have to pay? As we've discussed, you need to know what bank charges to expect so that you can ensure that you have money in the account to cover them. Ask your banker.

D. Who Must Maintain a Trust Account

Rule 43(a) requires all lawyers, who receive client funds or third-party funds in Arizona or in connection with representation of clients in Arizona, to maintain a client trust account. If you do not receive client or third-party funds, you may not need a client trust account.

No distinction is made based upon frequency of practice, so that those who practice full time are not required to keep more detailed records than part-time or occasional practitioners. A trust account must be maintained and all trust money deposited into that account. All lawyers must maintain the same minimum bank accounts and records. The only difference among practitioners will be the amount of work necessary to maintain those records, which will naturally be a function of the volume and the sophistication of the legal business conducted by each.

E. Approved Depositories For Trust Funds

The interest on IOLTA accounts is paid to the AZFLSE. Under the rule, the foundation uses the interest to fund "programs designed to assist in the delivery of legal services to the poor, for law-related education... and to fund studies or programs designed to improve the administration of justice." In existence since 1984, Arizona's IOLTA program currently provides more than $1 million per year for these purposes.

To be registered with the State Bar of Arizona, the Supreme Court of Arizona, and the foundation, it is necessary to complete an enrollment form. The enrollment form, instructions for completing the form, and the notice you can give to the bank can be found

at http://www.azflse.org/azflse/IOLTA/lawyersenroll.cfm#Forms. You must complete and return the enrollment form each time you open, close or transfer an IOLTA account.

If you have questions about completing the form, problems with your bank in setting up the account or questions about IOLTA requirements, please contact the Trust Account Hotline at the State Bar of Arizona at 602-340-7305.

If you have specific questions regarding interest rates or service charges, see the complete listing of approved participating banks at http://www.azflse.org/AZFLSE/iolta/allbanks.cfm.

Financial institutions are not required to participate in IOLTA. If an institution chooses not to participate, then lawyers who have attorney client accounts at that financial institution will have to transfer those accounts to institutions that do participate in the IOLTA program, since the financial institution will not be approved by the Supreme Court as a qualified depository for trust funds.

There are no tax consequences for the client or the lawyer as a result of IOLTA participation. Interest is earned on IOLTA accounts are remitted by the Bank to the AZFLSE and are not taxable to the client or to the lawyer. The lawyer is not required to prepare and file IRS 1099 forms, and neither the client nor the attorney is named as a recipient on any 1099 form. However, if a non-IOLTA account is opened under Rule 43(f)(3), then the interest will belong to the client and the lawyer will be required to prepare IRS 1099 forms for that client.

Normal bank service charges are paid from the interest earned by the IOLTA accounts. Check printing charges, wire transfer fees, bank checks or certified checks, and overdraft costs are not considered normal service charges and are not paid by the AZFLSE.

F. IOLTA or Separate Trust Account?

Rule 43, Ariz. R. Sup. Ct. requires lawyers to place client funds in a trust account, with placement of nominal sums or funds held for a short period of time in an IOLTA account. The rule states that a lawyer shall take into consideration the following factors when determining whether to deposit clients' funds into an IOLTA account or to open a separate interest-bearing account:

1. the amount of funds to be deposited;

2. the expected duration of the deposit, including the likelihood of delay in the matter for which the funds are held;

3. the rates of interest or yield at the financial institution where the funds are to be deposited;

4. the cost of establishing and administering a separate non-IOLTA account for the client's benefit, including service charges, the costs of the lawyer's services, and the costs of preparing any tax reports required for income accruing to the client's benefit;

5. the capability of financial institutions to calculate and pay income to individual clients; and

6. any other circumstances that affect the ability of the client's funds to earn a net return for the client.

The rule goes on to state, “No disciplinary matter shall be pursued by the state bar against any lawyer or law firm solely by reason of the making of a good faith determination of the appropriate account in which to deposit or invest client funds.”

The following guidance will help you make a good faith determination of whether the amount of interest an account will generate will justify the cost of opening and maintaining the account for the client. If the lawyer can earn net interest for the client, the lawyer must do so. In deciding what benchmark amount of interest a separate client trust account must earn to generate net interest, the lawyer should consider all costs associated with such an account.

These costs will be either directly or indirectly passed on to the client, so the client’s separate account must earn enough to justify its existence. Several cost factors to consider in this determination include:

Internal costs:

1. the expenses of the lawyer’s or law firm’s staff time in establishing a separate account;

2. the preparation and filing of tax forms (e.g. IRS 1099 forms);

3. the bookkeeping and accounting expenses for tracking the account;

4. the monthly reconciliation of the account for the client; and

5. closing the account and remitting the funds to the client

External costs:

1. the minimum balance requirement at the bank at which the account is placed;

2. the expense of ordering pre-numbered checks;

3. the service charges, if any, assessed against the account by the bank; and

4. other additional fees that the bank may have for investment policies

After an approximation of these costs has been made, this amount becomes the benchmark amount of interest. If a particular client's funds do not earn that benchmark figure, then the money should not be placed in a separate interest-bearing account for the client. If the funds cannot generate the benchmark figure, then the account will cost more in expenses than it will generate in interest income, so the funds should be placed in the IOLTA account. Such client funds are ones that are "nominal" or held for a "short period of time." If the client's funds can earn the benchmark figure or more, then the funds must be invested separately for the client. A few examples of applications of this benchmark figure follow:

1. A small firm or solo practitioner with relatively low overhead expenses may determine that a $80 figure is a reasonable approximation of the internal and external costs associated with setting up and maintaining a separate interest bearing account for the client.

Suppose a $15,000 check that is to be held for six months is received on behalf of a client. If this money were placed in an account bearing 1.5 percent interest, it would earn $110.96 Formula: $15,000 x 1.5% (rate paid on NOW accounts for illustration purposes only) divided by 365 x 180 days (time of deposit) = $110.96

This would justify a separate client account. But, if this same check were to be held for only two weeks, a separate account should not be set up because it would earn only $8.63.

2. A medium-sized firm may determine that a $120 figure is a reasonable approximation of the internal and external costs associated with setting up and maintaining a separate interest bearing account for the client. Suppose an $80,000 check that is to be held for two months is received on behalf of a client. A separate account should be set up because more than $197.26 in interest would be earned. But, if this same check were to be held for one week, the funds should be deposited in the IOLTA account since only $23.01 interest would be earned.

3. A large firm may determine that a $160 figure is a reasonable approximation of the internal and external costs associated with setting up and maintaining a separate interest bearing account for the client. Suppose a $150,000 check that is to be held for six weeks is received on behalf of a client. A separate account should be set up because $258.90

would be earned. However, if this same amount were to be held for one week, it should be placed in the IOLTA account since only $43.15 in interest would be earned.

A lawyer or firm must periodically adjust their benchmark amount of interest figure to accurately reflect changing costs in the determinative factors and the interest rate. As the examples illustrate, it is not just the amount of the client's funds that is decisive. A combination of the size of the funds, the duration that the funds will be held, and the current interest rate must be used to determine which client trust funds are to be deposited in the IOLTA account and which client trust funds are to be deposited in an account for the individual client.

The following table provides another answer to the practical question of what is "nominal in amount" or expected to be held for a "short period of time." For illustration, the table assumes that $100 is a reasonable estimate of the minimum amount of interest that a segregated trust account for an individual client must generate to be practical in light of the costs involved in earning or accounting for any such income.

Principal Deposit	Number of days required to generate $100 of interest at 1.5% compounded daily
$1,000	2500 days
$3,000	811 days
$5,000	487 days
$10,000	243 days
$20,000	122 days
$40,000	61 days
$75,000	32 days
$100,000	24 days

These examples based on simple interest are given as guidance. Lawyer s and firms should ensure that they perform their own calculations using the relevant numbers. The bank interest rate and the benchmark amount of interest for each individual lawyer or firm must be used for actual calculations.

For IOLTA questions, please contact the AZFLSE at http://www.azflse.org/azflse/about/contactus.cfm

G. Account Names

All funds of clients paid to a lawyer or law firm shall be deposited in one or more identifiable interest-bearing trust accounts. In the case of IOLTA accounts, the title should be "IOLTA Account." The word "IOLTA" should also appear on the firm's checks and deposit slips.

When you find it necessary or appropriate to establish a separate client trust account, in

addition to an IOLTA, the words “Trust Account” should still appear on the separate client trust account. Trust accounts should be established only in the name of a lawyer or law firm. There are four choices depending upon the nature of the lawyer’s employment. The client trust account should be established in the name of:

1. the lawyer;

2. a partnership of lawyers;

3. a professional corporation of which the lawyer is a member; or

4. the lawyer or partnership of lawyers by whom employed.

Whichever name is used, the designation “Trust Account” should also appear in the title of the account. Source documents, such as such as checks and deposit slips, should also bear the identical registration. This underlines the personal obligation of the lawyer to control client’s funds.

For example, where representation of a large collection client dictates that a separate trust account be set up, the following designation might be used:

Dee Fender
Client Trust Account
American Express – Collections

In connection with establishing separate interest bearing accounts, for example, to hold $50,000 for three months under a real estate contract, register as:

Dee Fender, Esq.
FBO[1] John Q. Public
Client Trust Account

The purpose of this suggestion is to ensure that interest is properly reported as taxable income to the client, and not the lawyer. Additionally, when establishing an account, it is critical to report the client’s tax identification number or social security number to be sure that the interest earned is taxed directly to the client. Where the interest is to be split between buyer and seller, two accounts should be opened in the name of each party with their respective social security numbers. This will ensure that each party will only pay tax on the interest attributable to each.

H. Proper Signatories

It is not prohibited by Rule that a non-lawyer can be a signer on the trust account; however,

[1] For the Benefit Of.

there are management decisions to consider. Since the lawyer is ultimately responsible for the supervision of staff, proper internal controls and due professional care, should you take the risk? Is it necessary to have a non-lawyer be a signer? Planning can often rule out the need for non- lawyers as signers. For example, if a filing fee must be paid, there is usually a document to be filed that the lawyer must sign; sign both at the same time.

The best advice is to never have an authorized signer on a trust account who does not have a law license to protect.

I. Responsibility For Establishing and Maintaining Proper Trust Accounts

A lawyer's fiduciary responsibilities are personal, non-delegable duties. ER 5.1(a), Rule 42, Ariz. R. Sup. Ct., states that a partner in a law firm, and a lawyer who individually or together with other lawyers possesses comparable managerial authority in a law firm, shall make reasonable efforts to ensure that the firm has in effect measures giving reasonable assurance that all lawyers in the firm conform to the Rules of Professional Conduct. The obligation, with respect to proper fiduciary responsibilities, requires every law firm maintain records and that all personnel are trained in the requirements. Furthermore, the obligation requires that those exercising fiduciary responsibilities be adequately supervised to ensure compliance. However, while others may be employed to assist in fulfilling fiduciary obligations, it is the lawyer and law firm alone that nears ultimate ethical responsibility.

J. FDIC Insurance

As noted earlier, a trust account should be maintained at a financially stable bank. But if the bank goes under, how do you ensure that your client trust account is treated as a fiduciary account for FDIC insurance purposes? You meet the FDIC requirements if you are complying with Rule 43, Ariz. R. Sup. Ct., which sets out client trust account requirements.

According to the FDIC, you must meet the following two requirements to qualify:

1. [t]he fiduciary nature of the account must be disclosed in the bank's deposit account records (e.g., "Jane Doe as Custodian for Susie Doe" or "First Real Estate Title Company, Client Escrow Account"). The name and ownership interest of each owner must be ascertainable from the deposit account records of the insured bank or from records maintained by the agent (or by some person or entity that has agreed to maintain records for the agent).

2. ["FAQs About FDIC Insurance," http://www.fdic.gov/deposit/deposits/insured/faq.html]

The first requirement is that your client trust account must specifically indicate that it is your client trust account, thus showing the fiduciary relationship. This also complies with Rule 43(a), Ariz. R. Sup. Ct. [See section G above.]

The second requirement is that you must maintain records showing "the interests of the parties in the account." You already must be maintaining such records to comply with Rule 43, Ariz. R. Sup. Ct. As a result, if you are keeping appropriate trust account records, you should have the appropriate information.

K. Is Help Available?

1. Ethics opinions, sample fee agreements, links, rules and other online IOLTA information: http://www.azbar.org/Lawyers

2. Arizona Foundation for Legal Services & Education:
   http://www.azflse.org/azflse/IOLTA/lawyersenroll.cfm

3. Trust Account Hotline, 602-340-7305:
   The State Bar of Arizona's trust account hotline provides information to Arizona lawyers, for prospective conduct related to trust account matters.

4. Practice 2.0, the State Bar's confidential practice management program
   602-340-7332
   http://www.azbar.org/practice20:
   Practice 2.0, the State Bar's practice management program provides confidential and individual management advice and consultations to the State Bar of Arizona members on all aspects of practice management, including assistance with setting up trust accounts.

5. Online Trust Account CLE:
   Law Practice Management & Technology - Managing Your Trust Account: Preparing for Random Trust Account Examinations:
   http://www.legalspan.com/AZBar/catalog.asp

6. Ethics hotline 602-340-7284:
   For prospective ethical questions related to ethical duties regarding receipt, deposit, management and disbursement of funds, whether trust account or not, call the Bar's ethics hotline.

SECTION V: FEES

Why is it important in a manual on client trust accounting to discuss what kind of fees you accept? Because the characterization of the fee – and, in reality, how you apply it to the client's work – determines whether you put the fee in your IOLTA account or your operating account.

Any funds received by a lawyer can be analyzed by the basic test of "To whom does this money belong right now?" If the answer is "the lawyer," the funds should be deposited to an operating account. If the answer is "the client" (or a third party related to the representation), the funds should be deposited to the trust account. If it belongs in part to the lawyer and in part to the client or third party, it must first be deposited into the trust account. The part belonging to the lawyer should be removed once the funds have been earned.

A. Advanced Fee

An advanced fee is an amount paid to a lawyer in contemplation of future services that will be earned at an agreed-upon basis, whether hourly or flat. Any amount paid to a lawyer in contemplation of future services is an advanced fee regardless of what the fee is called. An advanced fee must be deposited into the client trust account.

B. Flat Fee

A flat fee is a fixed amount paid to a lawyer for specific, agreed-upon services, or for a fixed, agreed-upon stage in a representation, regardless of the time required of the lawyer to perform the service or reach the agreed-upon stage in the representation. A flat fee is not an advance against the lawyer's hourly rate and may not be billed against at an hourly rate. A flat fee may or may not be paid in advance, but is not deemed earned until the work is performed.

A nonrefundable fee or earned-upon-receipt fee is a flat fee paid in advance that is deemed earned upon payment regardless of the amount of future work performed. The agreement as to when a fee is earned determines whether it must be deposited to the client trust account, and may have significance under other laws such as tax and bankruptcy. If a flat fee is not designated earned-upon-receipt, then it is presumed to belong to the client and it must be deposited in the trust account.

C. Retainer

"Retainer" denotes an amount paid specifically and solely to ensure the availability of a lawyer to perform services on behalf of a client and to preclude the lawyer from taking adverse representation. This amount does not constitute payment for any specific legal services, whether past, present, or future, and may not be billed against for fees or costs

at any point. A retainer becomes the property of the lawyer upon receipt, and should not be deposited into the client trust account.

What is often called a retainer, but is in fact merely an advance fee deposit, involves a security deposit to ensure the payment of fees when they are subsequently earned, either on a flat fee or hourly fee basis.

Lawyers often mistakenly use the word "retainer" to refer to advance fees. The account to which funds should be deposited is determined by ownership of those funds at the time they are received. This is defined by the fee agreement between lawyer and client. The best management procedure is to clearly define in a written fee agreement to whom the money belongs, where it will be deposited and how and when it will be used.

If the initial payment is defined as a "retainer" that will be paid for the lawyer's availability (including the potential necessity for the lawyer to decline representation of other clients), whether or not his or her services are actually used, the fee generally belongs to the lawyer upon receipt and should be deposited into an operating account.

If, on the other hand, the "retainer" is actually an advance of fees for services to be provided in the future, the fee at its receipt is the client's money and should be deposited into the client trust account.

D. Advanced Fees and Costs

All advanced payments of costs must be held in trust until the costs are incurred. If a lawyer receives an advanced payment that includes both fees and costs, the lawyer must deposit that payment into the trust account. The advanced fee portion may be disbursed when the funds become available, but the costs must be held in trust until incurred.

The reasonableness requirement and application of the factors to be considered may mean that a client is entitled to a refund of an advance fee payment even though it has been denominated "nonrefundable" "earned upon receipt" or in similar terms that imply the client would never become entitled to a refund. So that a client is not misled by the use of such terms, ER 1.5(d)(3) requires that a lawyer make certain minimum disclosures to the client in writing. This does not mean the client will always be entitled to a refund upon early termination of the representation nor does it determine how any refund should be calculated but merely requires that the client be advised that the client may be entitled to a refund based upon application of the factors in ER 1.5(a) that determine the reasonableness of a fee. Lawyers should keep time records for all representations, even flat-fee arrangements and contingency cases, so they can use this information if they need to demonstrate the reasonableness of the fee in case the client terminates representation early.

E. Contingent Fees

ER 1.5(c) requires that contingent fee agreement be in writing and signed by the client. The agreement must state the method by which fee is to be determined, including the percentage that lawyer receives if settlement, trial or appeal, and whether the expenses will be deducted from the recovery before or after fee is calculated. The agreement must clearly notify the client of expenses client is responsible for whether client is the prevailing party. Upon conclusion of matter the lawyer must provide the client with a written statement stating the outcome, the remittance to client (if any), and the method of determining any remittance. This written statement is not a substitute for a client ledger.

SECTION VI: DEPOSITING MONEY INTO YOUR CLIENT TRUST ACCOUNT

A. What MUST go into your client trust account?

The rule is that when you receive *any money* that your client has an interest in, it must be deposited into the client trust account and *cleared* before it can be paid out.

Money "received or held for the benefit of a client" includes:

- Money that belongs to the client outright (e.g., advances against fees);
- Money in which you and your client have a joint interest (e.g., settlement proceeds that include your contingency fee);
- Money in which your client and a third party have a joint interest (e.g., money you hold for a partnership of which your client is a partner or settlements that will be used to satisfy medical liens); and
- Money that doesn't belong to your client at all but which you are holding as part of carrying out your representation of the client (e.g., when your client has commenced an action for interpleader).

You should note that this rule *doesn't* include non-refundable retainer fees taken not for services to be rendered but solely to ensure your availability to the client. Since these retainers are completely earned the moment you receive them, they are your money, not your clients', and therefore you should never deposit them into your client trust account; however, sometimes your client will give you a single check that includes both a non-refundable retainer fee and money that you will hold for the client, like an advance against costs and expenses. Funds belonging in part to a client or third party and in part to the lawyer must be deposited, intact, into the trust account. In this case, deposit the check into your client trust account and write yourself a check for the retainer fee portion as soon as the check clears and the money becomes available, leaving only the money for the costs and expenses in the client trust account. Under these circumstances, it might be simpler to have the client write two checks; one for your non-refundable retainer and another for client costs and expenses.

B. What MAY go into your client trust account?

There is only one type of money that *may* be deposited into your client trust account: Funds to pay service or other charges or fees imposed by the financial institution. Everything else either *must* or *must not* be deposited into the account.

Bank charges. As we've mentioned, ER 1.15(b) says you are allowed to deposit out of your own money "funds to pay service or other charges or fees imposed by the financial institution, but only in an amount reasonably estimated to be necessary for that purpose may be deposited therein." The rule *allows* you to keep your own money in the account to cover bank charges; it doesn't *require* you to. However, if you do not keep your own funds in the client trust account, you run the risk of converting other client funds if any service charges or fees are assessed against that account. Sooner or later, every lawyer incurs a bank service charge. Whether the charge is for printing checks, a monthly service charge, the cost of issuing or receiving an electronic transfer, a returned deposit item, a returned check item or some other special charge, bank charges must be dealt with.

If you deposit your own money into your client trust account to cover the charges, you may be concerned about how much is "reasonably estimated to be necessary." That depends on the kind of bank charges you expect and how often you expect to incur them. Talk to your banker and get an estimate of what you will be charged.

There are two ways to properly account for bank charges. The first is simply to arrange with the financial institution to charge another account (e.g., the business account or personal account) whenever a charge is incurred by the lawyer trust account. For some practitioners, this arrangement works fine, in which case there is no trust recordkeeping necessary, since the charges are not made to, but are handled outside of the trust account. Occasionally, however, practitioners experience problems with this arrangement due to the normal turnover of banking personnel when a new manager forgets (or was never told) to charge a business or personal account for check printing charges and so the client trust account is assessed of the bank charges.

A second method eliminates any problem of bank personnel turnover and gives the lawyer complete control. That method calls for the attorney to prepare a client trust ledger showing the lawyer as the "client" and the matter as "Bank Charges." The lawyer then deposits a "reasonably" small amount of personal money in the trust account and reflects it on the ledger card marked for "Bank Charges." Charges are then recorded and written off against the ledger as they are incurred. When the running balance on that ledger sheet becomes low, a new, small deposit of personal funds is made to bring the balance up to a comfortable level. Remember that a deposit of your own money to cover bank charges, like every deposit you make to your client trust account, ***must*** **be properly recorded** on the general ledger/checkbook register for your client trust account, and a special "Administrative Funds/Bank Charges" ledger.

Some very well intentioned lawyers have mistakenly thought that they could keep a cushion of their own funds in the trust account in case they made a bookkeeping error and did not have enough money in the trust account. The Rules prohibit for such a cushion and it is considered to be commingling.

C. What MUST NOT go into your client trust account?

Rule 42, ER 1.15(c) says that, other than money to cover bank service charges, you "shall deposit into a client trust account legal fees and expenses that have been paid in advance, to be withdrawn by the lawyer only as fees are earned or expenses incurred." Unless one of your clients has an interest in the money, keep it out of your client trust account. **NEVER** put your personal or office money, including funds like employee payroll taxes, into your client trust account. Do not deposit funds belonging entirely to the lawyer (e.g., fees that are already earned) or funds **not** related to representation of a client (e.g., funds you hold as treasurer of your professional association).

D. What about credit card payments?

Lawyers who choose to accept credit card payments for advance fees, costs or expenses must comply with the procedures and requirements for Rule 43(b)(3) and ER 1.15(b).

A lawyer or law firm may permit funds from a credit card transaction to be deposited into a client trust account for payment of advance fees, costs or expenses, and merchant or credit card transaction fees, but only if the lawyer has sources of funds, other than client or third-party funds, available at the time of the credit card transaction to replace any funds that may be debited from the account due to a credit card chargeback and any associated fees or charges. Permitting the deposit of funds from a credit card transaction into a client trust account for payment of advance fees, costs or expenses, and merchant or credit card transaction fees is at the risk of the lawyer permitting the deposit.

If a debit is made from a lawyer's or law firm's trust account due to a credit card chargeback, the lawyer permitting the deposit must, within three business days of receipt of notice or actual knowledge that a chargeback has been made, act to protect the property of the lawyer's or law firm's clients and third persons by depositing into the trust account his or her own funds in an amount equal to the amount of the chargeback that exceeds the client's credit card funds remaining in the trust account, and any fees or charges associated with the chargeback.

Remember, the fact that money was received via a credit card does not change the character of the funds. In other words, if you receive an advance against fees to be earned in the future, that money still needs to be deposited to you trust account because it belongs, at the time received, to your client.

Banks will usually charge the lawyer a percentage of the credit card amount as a fee. For example, on a $1,000 charge, the bank may charge the lawyer $40. A client may agree to pay the credit card fees, so long as the fees are reasonable and so long as the agreement is recorded in writing, usually in a fee agreement. Without any agreement by the client indicating otherwise, such a charge is considered an expense to the lawyer and is not chargeable to the client.

E. Limited-Risk Deposit Exceptions

As discussed in Section II, Rule 43(b)(4) allows for disbursements to be made against four categories of "limited-risk uncollected deposits." You may disburse against uncollected funds if the deposit is a limited-risk uncollected deposit, you have personal funds available to cover the deposit in the event the deposit is returned or fails for any reason, and such correction can occur within three business days of learning of the failed deposit.

The first thing to determine is whether or not the deposit meets the criteria of a "limited-risk uncollected deposit." Is it a:

- Certified check
- Cashier's check
- Bank check
- Official check
- Treasurer's check
- Money order
- Other instrument in which the payor is a bank, savings and loan association, or credit union
- Check issued by United States or the State of Arizona or any agency or political subdivision of the state
- Check or draft issued by insurance company, title insurance company, or a licensed title insurance agency authorized to do business in this state.

You will then need to determine if you have personal funds available to cover the deposit if, for any reason, the limited-risk deposit is returned against the trust account. You need to determine if the personal funds will be available to be deposited into the trust account within three business days of learning of the deposit failure. **If you fail to personally pay the amount of any failed deposit within three business days of receipt of notice that the deposit has failed, you will be found to have committed ethical misconduct based upon the disbursement of uncollected funds.**

F. Disputes With a Client

If there is a dispute between you and your client regarding the ownership of money in a trust account, then you must keep the money in the trust account, and take timely steps to resolve the dispute.

Such a situation occurs, for example, where a lawyer receives an advance fee of $2,500. A dispute can arise between the lawyer and the client if the lawyer believes he is entitled to take out $1,500 from the advance fee in the trust account, but the client has a different point of view, claiming that the lawyer did not do any work. Faced with such a dispute, the lawyer cannot take out the $1,500. Rather, he must leave the money in the trust account

and must take steps to resolve the dispute via negotiation with the client, mediation, or fee arbitration. As a last resort, the lawyer would need to initiate an action to determine who is entitled to the money.

If a portion of the amount held in trust is not disputed, then the lawyer must promptly disburse that amount to whomever it is owed.

G. Disputes With Third Parties Over Funds in a Trust Account

If a lawyer holds money of a third party in his trust account and a dispute arises over what should be done with that money, then the lawyer must keep the disputed amount of money in the trust account, until one of the following occurs:

1. the parties reach an agreement on the distribution of the property;

2. a court order resolves the competing claims; or

3. distribution is allowed under ER 1.15(f).

H. Third-Party Claims to Funds in a Trust Account

Third parties, such as a client's creditors, may have just claims against funds in the trust account. Life can get even more difficult for a lawyer when the lawyer's client disagrees with the third-party as to how the money should be distributed. Because the lawyer is a fiduciary to the third party as well as to his client, the lawyer may have a duty to protect such third party claims against wrongful interference by the client. Therefore, the lawyer may refuse to surrender the funds or property to the client. This situation arises most commonly when medical providers notify a lawyer that their medical expenses should be paid out of any settlement for the client.

If the dispute is between a client and a third-party claimant, ER 1.15(f) now allows the lawyer to provide written notice to the third party of the lawyer's intent to distribute the property to the client as follows:

1. The notice shall be served on the third party in the manner provided under Rules 4.1 or 4.2 of the Arizona Rules of Civil Procedure, and must inform the third party that the lawyer may distribute the property to the client unless the third party initiates legal action and provides the lawyer with written notice of such action within 90 calendar days of the date of service of the lawyers notice.

2. If the lawyer does not receive such written notice from the third party within the 90-day period, and provided that disbursement is not prohibited by law or court order, the lawyer may distribute the funds to the client after consulting with the client regarding the advantages and disadvantages of disbursement of the disputed

funds and obtaining the client's informed consent to distribution, confirmed in writing.

3. If the lawyer is notified in writing of an action filed within the 90-day period, the lawyer shall continue to hold the property separate unless and until the parties reach an agreement on distribution of the property, or a court resolves the matter.

4. Nothing in the rule is intended to alter a third party's substantive rights.

SECTION VII: PAYING MONEY OUT OF YOUR CLIENT TRUST ACCOUNT

Before you write your first client trust account check, there are things you should know.

A. What payments CAN you make?

You can make any payments **on behalf of your client** out of your client trust account, including paying client costs and expenses (e.g., court filing fees or deposition transcript costs), disbursing settlement proceeds, paying yourself earned and undisputed legal fees, etc. You may also pay bank charges for the account. Those are the *only* payments you're allowed to make out of your client trust account.

Bank charges. For individual (non-IOLTA) client trust accounts, paying bank charges is simple:

Since all of the charges are incurred for the client for whom you have the account, you can pay the charges out of that client's money.

For IOLTA accounts, paying bank charges is a little more complicated. When the bank charges for a service (e.g., for wiring money) for a specific client, you can treat the charge as you would any other cost and pay for it out of money you are holding for that client in the account. But some charges, like check-printing charges, aren't specific to a certain client. Like all your other general operating expenses, you – not your clients – have to pay these charges. That's why ER 1.15(b) and Rule 43(a)(1) and (2) allow you to keep a little of your own money – an amount reasonably sufficient to cover service fees, other bank charges, merchant fees or credit card transaction charges – in your client trust account.

B. What payments CAN'T you make?

You *can't* make payments out of your client trust account to cover your own expenses, personal or business, or for any other purpose that isn't directly related to carrying out your duties to an individual client. You also can't pay money out of your client trust account on behalf of a client if the client doesn't have money available in the trust account to cover those payments.

You should also remember that you can't pay yourself legal fees that your client is disputing, whether or not you feel you've earned them. The moment a client disputes your fees, the disputed amount is frozen in your client trust account until the dispute is settled. When the amount of your fees is no longer in dispute, you have an ethical obligation to take those fees out of the client trust account as soon as you reasonably can.

C. How MUST you make payments?

You must always pay out money from your client trust account only by using a pre-numbered check or electronic transfer. You should never pay out money in cash, money orders, cashier's checks, or with checks or other instruments made out to cash because **you have no evidence of payment.**

You may also disburse through phone and internet transfers. While not prohibited by the rules, these transactions are not recommended because of the increased potential for fraud. Making disbursements through phone or Internet transfers is at the risk of the lawyer making the disbursement. If you choose to use these methods, be meticulous with your recordkeeping to ensure a proper audit trail. Make sure that these transactions are properly recorded on the corresponding client ledgers and general ledger/checkbook register along with the confirmation number. Additionally, all instruments of disbursement shall be identified as a disbursement from a trust account. Rule 43(b)(5).

Some lawyers carry blank client trust account checks around to pay client costs and expenses that come up when they're out of the office. Don't. This is a bad practice, which results in checks being written out of numerical order (i.e., lower numbered checks being dated later than higher numbered checks), and, more often than not, a few checks disappearing altogether. That can make it hard to keep orderly records and reconcile your books. If you're out of the office and a client expense comes up, pay it out of your general office account and, when you get back to the office, write a client trust account check to reimburse yourself.

D. Who SHOULD make payments?

Your clients have entrusted *you* with their money, and you are personally accountable for it. Giving other people access to your clients' money is even riskier than giving them access to your own money. If your money is stolen because you trusted the wrong person, all you lose is the money. If your clients' money is stolen because you trusted your employees or your spouse to sign client trust account checks, you can lose your clients' money, your professional reputation and even your license to practice law. *Don't* make a signature block or stamp for your client trust account checks; *don't* pre-sign blank client trust account checks. If you do, sooner or later some of your clients' money will be missing, and whether the cause is dishonesty or incompetence, you will bear responsibility for both the financial loss and the violation of your fiduciary responsibility.

E. When MUST you make payments?

You must "promptly deliver … to the client" money which the client is entitled to receive. This means that if your client asks you to return money you are holding in trust for that client, you must deliver that money promptly. Often, a client request for payment is triggered by notice from you that certain money has been received for the client, such as settlement proceeds. ER 1.15(d) requires that you "promptly notify a client" about the

receipt of any client funds. What is meant by “promptly” for purposes of both notifying clients about funds received and making payment as requested by clients will depend upon the specific circumstances of each client’s matter.

Lawyer fees. When you’re holding client money that includes your undisputed fees, you have to take those fees out of the client trust account promptly after you’ve earned them. Make sure though, that your bank has collected the funds.

Third-party claims. You also may have a duty to promptly pay costs and expenses owed to a third party incurred on behalf of a client. In some cases, the client may dispute a third party’s claim to the money. This situation most often arises in connection with a medical lien, which the attorney and client have both signed. After the recovery is received, the client instructs you not to pay the doctor. Because you signed the lien, turning the funds over to the client may expose you to potential civil liability and may violate your fiduciary duty to the doctor. On the other hand, paying the doctor against the express instructions of the client also presents difficulties. You now have an option under ER 1.15(f) to notify the third party that you intend to distribute the funds to the client. You must give the third party written notice of your intent, serve it pursuant to Rule 4.1 or 4.2 of civil procedure rules, and allow the third party 90 days to notify you of any actions the third party plans to take. If you receive notice from the third party, then you must continue to hold the funds; if you do not receive notice from the third party, then you may distribute the funds to the client after getting the client’s informed consent, in writing, to do so. This rule is not intended to alter a third parties substantive rights.

F. Check 21

On October 28, 2004, the Check Clearing for the 21st Century Act (commonly known as “Check 21") went into effect. This federal law enables banks to handle more checks by electronic transmission, which should make check processing faster and more efficient. Today, banks often must physically move original paper checks from the bank where the checks are deposited to the bank that pays them. This transportation can be inefficient and costly. Check 21 allows banks to capture a picture of the front and back of the check along with the associated payment information and transmit this information electronically. If a receiving bank or its customer requires a paper check, the bank can use the electronic picture and payment information to create a paper “substitute check.” This process helps banks to reduce the cost of physically handling and transporting original paper checks, which can be costly.

Check-processing speeds should continue to increase over time, as banks make further operational changes in response to Check 21. That means money may be deducted from your trust account faster. One result of faster check processing will be a much shorter gap between the time you disburse funds for payment and the time the covering funds are withdrawn from your trust account (known as the "float" time). With Check 21, a disbursement may be processed in a matter of hours or even minutes, so you cannot safely assume you have a grace period after writing a check before the funds are actually

disbursed from your trust account. In terms of timing, using a substitute check under Check 21 will eventually result in a total transaction time almost as quickly as using a debit card.

Another federal check law (Expedited Funds Availability Act) specifies the maximum times by which your bank must make funds available to you, though most banks make funds available faster than required. You may not get access to the funds from checks you deposit any sooner, because Check 21 does not shorten check hold times. Generally, banks can hold local checks for up to two days, out-of-town checks for up to five days, and other types of checks (e.g., checks over $5,000, checks drawn on new accounts, checks written against consistently overdrawn accounts) for up to thirty days. Checks you write could clear in hours or even minutes, increasing the risk that a check will bounce if funds are not in the trust account when you write the check. You should not write a check from your trust account unless the funds are already in the account to cover it.

Also, under Check 21, banks will no longer be required to return your canceled checks; they may return “substitute checks” instead. A “substitute check” is the legal equivalent of the original check if it accurately represents the information on the original check and includes the following statement: “This is a legal copy of your check.” You can use it the same way you would use the original check. A bank must also have handled the “substitute check.” Check 21 will not explicitly require banks to provide “substitute checks,” so you may want to check with your bank to review their policies. These copies will have the same evidentiary standing in courts of law as the originals. Although banks may allow you to view and print out images of their checks over the Internet, those self-printed copies will not technically be considered substitute checks even though most courts will likely still accept them as evidence of payment. Certain substitute checks will be legally equivalent to an original check for all purposes under state and federal laws. However, the substitute check will not be as useful as the original check for proving forgery or alteration, because it can't be used to determine pen pressure, and it is less useful for handwriting analysis.

Although Check 21 went into effect on October 28, 2004, banks do not **have** to begin electronically clearing checks on that date, Check 21 **authorizes** banks to begin use of electronic check clearing. Most major banks already have imaging technology in place, but not all banks do, so some banks may continue to process checks the "old" way until they upgrade their processing systems. Check with your bank to determine whether they are processing checks according to Check 21.

Another provision of Check 21 will speed up resolution of a customer claim regarding fraud and error. Currently, banks do not need to credit the account of a customer who complains of error or fraud until their investigations are complete. After Check 21, banks must prove within ten days that disputed transactions were not their fault. If they do not provide such proof, they must credit a customer’s account for the disputed amounts even if they have not completed their investigations.

So, what do you do to avoid getting bounced? Stick to the rules:

ER 1.15(a) and Rule 43(b)(2)(A), Ariz. R. Sup. Ct. Maintain complete records of the handling maintenance and disposition of all funds of a client that come into your possession.

Rule 43(b)(1)(B) and (C). Ensure that employees and others assisting you are competent and properly supervised. Maintain internal controls within your office to safeguard funds held in trust. Record all transactions promptly and completely. You need to stay on top of which checks have cleared your account and when. You also need to be aware of when checks made out to you have been processed. Tracking your account online is probably the easiest way to stay up to date on your finances. Most banks allow you to view your account online for free. That way you can check your balance, see when your checks clear and see your recent transactions.

NOTE: This is not foolproof. Banks say the information is advisory, not necessarily accurate. If you are not sure how frequently your bank updates online account summaries, call them to find out so you know how current your online account information is.

Rule 43(b)(2)(B), (C) and (D). Maintain an account ledger or the equivalent for each client for whom monies have been received in trust, showing the date and the amount of each receipt and disbursement and any unexpended balance. Complete a monthly three-way reconciliation of the individual client ledgers, trust account general ledger/checkbook register, and trust account bank statement. Retain all trust account statements, canceled pre-numbered checks (unless recorded on microfilm by a bank or other financial institution), other evidence of disbursements, duplicate deposit slips, client ledgers, trust account general ledger/checkbook register, and reports to clients.

Rule 43(b)(4). Except for disbursements made from any of the four limited-risk uncollectible deposits, you may not disburse funds held in trust unless the funds are collected funds. A reliance on deposits that are not yet collected, unless considered a limited-risk deposit, that results in funds of clients being used, endangered or encumbered, will be grounds for disciplinary action.

Bank Clearing Process

Deposit
Check
(1)

Federal Reserve
Depository
(2)

Receive
Credit
(4)

Federal
Reserve
Collection
(3)

SECTION VIII: RECORDKEEPING

Some lawyers have the misconception that they cannot fulfill their ethical responsibility to keep track of their clients' money without spending a great deal of money on computer hardware and software that they will then have to spend a great deal of time learning how to use. While this is not true, technology can certainly make the process easier, particularly for lawyers and firms that have a high volume of trust account transactions.

ER 1.15, and Rule 43, Ariz. R. Sup. Ct., do not mandate any particular client trust-accounting system. (However, keep in mind that these Rules do spell out the particular records you must maintain.) You can hire consultants to set up a system, buy computer accounting software—whatever works for you—as long as you get the results and keep the records that the Rules require. If your client trust-accounting system will accomplish what our client trust accounting system does, then it's probably acceptable. However, whatever size firm you work in and whatever client trust-accounting system you use, you still have full personal fiduciary responsibility for accounting for your clients' money.

Keeping records is the way you do the "accounting" part of client trust-accounting. Record-keeping must be done consistently and keeping incomplete records is just as great a breach of your ethical responsibility as keeping no records at all. Plus, you are now presumed to have failed to safeguard client funds if you don't keep the required records. Rule 43(d)(3).

There are a few things that must be kept in mind in formulating procedures for handling the trust account, whether the lawyer uses a manual or a computerized system. These are:

- The lawyer may delegate duties, but cannot delegate responsibility or accountability for the trust account. Therefore, the lawyer must:
    - understand the types of records that must be maintained and how a trust account operates to properly train and supervise employees who maintain the account;
    - train all employees who will handle trust account functions;
    - supervise all employees who will handle trust account functions on an ongoing basis, not just when they are new; and
    - review trust account records regularly, including bank statements, the general ledger/checkbook register, deposit slips, individual client ledgers, etc.
- The lawyer or firm must establish and rigorously follow good internal control procedures. This includes:
    - don't make the same person responsible for receiving funds, recording funds and disbursing funds;
    - special precautions for handling cash;
    - the lawyer must be part of the internal controls system;

- taking specific steps to reduce the risk of misappropriation;
- not assuming that any individual will be impervious to temptation;
- monitoring and enforcing use of the established internal control procedures; and
- analyzing the potential effect on internal control procedures of downsizing, redistribution of duties or replacement of staff members and modifying procedures as necessary to compensate.

In establishing the system for maintaining the trust account, there are also some procedures that must be included, whether the system is manual or automated.

- Every transaction must be recorded in full detail, including date, payee of funds disbursed/payor of funds deposited, applicable client, check number, amount, reason for disbursement or deposit, etc.

- A current balance must be available at all times, both for the trust account as a whole and for each individual client on whose behalf money is being held.

- A ledger (or its equivalent) must be kept for each individual client whose money is being held that indicates the full history of that client's funds, including receipts and disbursements until the last penny has been paid from the account.

- A three-way reconciliation of the account must be performed no less frequently than monthly.

- Compare client ledgers to the general ledger/checkbook register. The total balance of all client ledgers should match the total on the general ledger/checkbook register.

- Reconcile to the bank statement, adjusting for outstanding checks, deposits in transit, bank charges, etc.

- Resolve any discrepancies immediately – they are usually easy to find if they are isolated to the period since the last bank statement and much more difficult to find as time passes.

- Make sure you have contact at least once a year with all clients whose funds are being held in your trust account – it can be time-consuming and difficult to find them if they have moved and the postal forwarding order has expired.

As we've discussed, Rule 43(b) requires you to keep two kinds of records: records created by the *bank* that show what went into and out of your client trust accounts; and records created by *you* to explain the transactions reflected in the bank documents.

A. How long MUST you keep records?

ER 1.15(a) and Rule 43(b)(2)(A) require you to keep trust account records for a period of five years after termination of the representation of that specific client.

B. Where MAY you keep your records?

If you have a practice involving a lot of clients, you have to hold onto a lot of paper. Because office space is limited and expensive, you may find that it makes more sense to keep some client-trust accounting records off-site rather than in your office. Assuming that you've taken appropriate steps to ensure that the records are in a safe location and that client confidentiality is preserved, there is not a problem with off-site storage - as long as you can produce the records within a reasonable time after receiving notice that you're the subject of a disciplinary inquiry (or need the records for some other reason, such as responding to a former client's inquiry). If you store files, label each box with the names of the client trust accounts the records to which they apply and the dates covered by the records. Also keep an index listing the names of all the boxes you send into storage. Otherwise, you're going to have to retrieve all the boxes from storage and sort through all the records they contain in order to respond to the disciplinary inquiry. This can be expensive, time-consuming, and, if you have to request a time extension, can create the wrong impression.

C. What if you HAVE a computerized system?

Even if you have a computerized accounting system, *you need to generate and keep hard copies of all the records required by the Rule* (including bank-created records). You can use computer printouts instead of hand-written ledgers for the records you are responsible for creating, but just having the data on a disk is risky. (It's a good idea to have these printouts dated and signed by the preparer to show when and by whom they were generated.) Remember that there are numerous computerized systems and no one knows how everyone works. Your records must be accessible and understandable to any investigator.

If you're using a computerized accounting system, you should remember that computer data can be lost through natural disaster (like earthquake or fire), power or equipment failure and human error. For your own protection, make hard copies regularly and have all of your computer records regularly backed up onto disks.

Beyond preservation of the computer data, you also should be very careful when changing or upgrading your specific accounting software application, your overall computer operating system, and the computer hardware itself. Different software applications and newer versions of the same software application may not be fully compatible with the data generated by your current software application. Similarly, changing computers or operating systems can cause difficult compatibility problems. These days, it is not unusual for computer technology to advance dramatically in a five year time period, rendering

some application data obsolete and problematic to use.

D. Which bank created records do YOU have to keep?

You are required to keep two kinds of bank created records: client trust account statements and canceled checks. Some lawyers don't take their duty to keep bank-created records seriously because they can always get copies from their bank. If your bank fails, merges with or is taken over by another bank, you may find that copies of your four-year-old canceled client trust account checks just aren't available. As previously noted, finding a bank that still offers "canceled checks" may take some searching and if you're unable to find such a bank, be sure to access and maintain "canceled check" information by requesting check imaging or other documentation from your bank. The Rules state that you do not have to keep copies of canceled checks that are recorded on microfilm by your bank, but bear in mind that the possible expense of obtaining numerous copies of canceled checks can be very costly.

E. How SHOULD you file bank-created records?

To ensure that you have a complete set of bank-created records, and to save you time when you need to find a particular record, you should have a simple, consistent filing system. One good system is to keep separate binders for each of your client trust accounts. Each binder should have one section for bank statements, one section for canceled checks, one section for deposit slips and one section for checkbook stubs. File each record in date order in the appropriate section of the binder for the account they refer to. Just label each binder with the name of the client trust account and the period it covers, and you should be able to find any record in one or two minutes.

An even simpler recommendation is to keep deposit slips and canceled checks in the same envelope as the bank statement to which they are associated, or print these documents using online account access and attach them to a copy of the bank account statement.

F. What records do YOU have to create?

You need to create three kinds of records to show that you know **at all** times what you're doing **with** your clients' money. We'll discuss each of these records in detail below, but a few general points apply to all of them:

ER 1.15(a) and Rule 43(b)(2)(A) require you to retain these records for a minimum of five years after the representation ends.

NEVER round off figures in these records. You must keep "complete records of such account funds." That means all receipts and payments must be recorded to the penny. These records can be handwritten, typed or printed out from a computer file. However, they should be complete, neat and legible, and stored in such a way that you can find

them—and read them—as many as five years later. Handwritten records should be kept *in ink—not* pencil or magic marker—in bound accounting books, and typed records or computer printouts should be filed in binders. As with bank-created records, you can save yourself time and trouble by labeling the covers of the books and binders with complete account or client names and the dates the records cover.

All deposits and payments should be recorded in the general ledger/checkbook register and client ledger as soon as possible. Waiting longer increases the chance that you will forget to record a transaction or will record it incorrectly. It also means that your records aren't up-to-date and that you might be spending money your clients don't have.

You must also keep your client trust account deposit slips and checkbook stubs so you will have a complete audit trail. These records will make it much easier to balance your books and to show what you did with your clients' money.

The client ledger. You must keep, create and maintain a client ledger or its equivalent for each client (for example, a break-out by client created by your computerized program) whose money you hold. This client ledger must give the name of the client, detail all money you receive and pay out on behalf of the client, the name of the payor of funds deposited or payee of funds disbursed, and show the client's balance following every receipt or payment.

Maintaining a client ledger is like keeping a separate checkbook for each client, regardless of whether or not the client's money is being held in your common client trust account. The only difference between properly maintaining a client ledger and properly maintaining your personal checkbook is that you can be disciplined if you fail to properly maintain your client ledger.

Every receipt and payment of money for a client must be recorded in that client's client ledger. For every receipt, you must list the date, the amount, purpose and payor (the source) of the money. For every payment, you must list the date, the amount, the payee (to whom the payment went) and purpose of the payment. After you record each receipt, you must add the amount to the client's old balance and write in the new total. After you record each payment, you must subtract the amount from the client's old balance and write in the new total.

Client: Alpha, A				Matter: 111111		
R	**Number**	**Date**	**Description of Transaction (Payor/Payee)**	**Payment**	**Deposit**	**Balance**
	Deposit	12/15/2016	Deposit Alpha – fees		$250.00	$250.00
	1001	01/17/2017	Dee Fender, Esq. – earned fees	$250.00		$0.00

When you deposit more than one check at a time for a client (i.e., using one deposit slip for all the checks), you should record the name of each client in your general ledger/checkbook register, as well as on the deposit slip. If you don't, it will be harder to reconcile your books and to answer any questions that may come up later.

You will find it much easier to keep your records straight if you don't put more than one client's records on a given page. You also shouldn't use the front of a page for one client and the back of the page for another. This means wasting some paper, but it will enable you to file all the client ledger pages that refer to a given client in chronological order and find those pages faster if you need them. If you're handling more than one case for the same client, you should maintain a separate client ledger for each matter. NOTE: Use special caution when dealing with multiple matters for the same client. Each matter should be uniquely identified and always use the same identification for the particular matter on all documents referencing it so there will be no confusion.

Administrative Funds Ledger. ER 1.15(b) and Rule 43(a)(1) say that you are allowed to deposit your own money to pay bank service charges or fees on that account, but only in an amount necessary for that purpose. The rule *allows* you to keep your own money in the account to cover bank charges; it doesn't *require* you to. Some lawyers arrange with the bank to have those charges assessed against their generating or personal accounts.

If you deposit your own money into your client trust account to cover the charges, you may be concerned about how much is reasonably sufficient. That depends on the kind of bank charges you expect and how often you expect to incur them. For IOLTA accounts, there are other kinds of bank charges you may incur, including charges for printing checks, for checks that are deposited in the account and returned for insufficient funds, and for transferring money by wire, etc. You need to know what these charges are so you can make sure that you always have enough money in the account to cover them.

When the bank charges for a service (e.g. for wiring money) for a specific client, you can treat the charge as you would any other cost and pay for it out of money you are holding for that client in the account. But some charges, like printing checks, aren't specific to a certain client. Like your other general operating expenses, you – not your clients – have to pay these charges. That's why the rules allow you to keep a little of your own money – an amount "for the sole purpose of paying bank service charges on that account, but only in an amount necessary for that purpose" – in your client trust account.

Remember that a deposit of your own money to cover bank charges, like every deposit you make to your client trust account, *must* be properly recorded in the general ledger/checkbook register for your client trust account, and a special "Administrative Funds" ledger. You should keep the "Administrative Funds" ledger the same way you keep your individual client ledgers, recording every deposit, every charge the bank makes against the account, and the running balance of money you have left to cover the charges.

Client: Administrative Funds, Dee Fender. Esq.				Matter: 999999		
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	12/01/2016	Deposit to open account – Fender		$50.00	$50.00
	Bank Fee	07/18/2017	Client Epsilon Returned Deposit Fee	$5.00		$45.00
	Deposit	07/31/2017	Client Epsilon reimbursement for $5 returned deposit bank charge		$5.00	$50.00

The general ledger/checkbook register. This is a written journal for each client trust account. You must keep track of the money going in and out of a client trust account on a general ledger/checkbook register, and give the account balance after each receipt or payment. When you have a trust account that's designated solely for one client's money, the general ledger/checkbook register will be identical to the client ledger.

Maintaining a general ledger/checkbook register is the only way you can know how much you have in the account at any given time. If you maintain the general ledger/checkbook register properly, you will not overdraft the client trust account unless there is a bank error.

In the general ledger/checkbook register, you must record every deposit into and payment out of the client trust account. For every deposit, you must record the date you deposited the money, the payor (source) of the funds deposited, and the amount of money you deposited. After you record each deposit, you have to add the amount to the account's old balance and write in the new total. For every payment, you must list the date, the payee of the funds disbursed, and the amount of the payment. After you record each payment, you have to subtract the amount from the account's old balance and write in the new total. Although it's not required by the rule, you will find it a lot easier to balance your books if you also record the client name and number of the check.

General Ledger/Checkbook Register						
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	12/01/2016	Deposit to open account – Fender		$50.00	$50.00
	Deposit	12/15/2016	Deposit – advanced fees – client Alpha		$250.00	$300.00
	1001	07/17/2017	Dee Fender, Esq. – earned fees – client Alpha	$250.00		$50.00
	Bank Fee	07/18/2017	Client Epsilon Returned Deposit Fee	$5.00		$45.00

	Deposit	07/31/2017	Client Epsilon reimbursement for $5 returned deposit bank charge		$5.00	$50.00

After taking into consideration the above requirements, a lawyer has numerous choices for software programs to computerize trust account procedures. The lawyer should consider the volume of transactions, the amount of money he or she can or is willing to spend on software and the hardware that will run it, the computer skills of the lawyer and of all staff members who will be assisting, and the availability and cost of training in his or her community.

Most of the complicated timekeeping/billing software being used by medium and large firms includes modules for handling the trust account. Because staff members are already trained on the basics of the timekeeping/billing product and the module is designed to work in an integrated fashion with the main program, firms will typically utilize a module for trust accounting.

G. Automated Alternatives to Managing Your Trust Account

Automating your trust account recordkeeping process can reduce the amount of data entry and calculation errors. You can search and find trust account information quickly, and perhaps from remote locations. Automating can organize the routine process of maintaining your trust account. It can save you space, but ALWAYS print copies of your client ledgers, general ledger, and monthly three-way reconciliation.

Keep in mind that most automated systems, have a built-in *two-way* reconciliation between the bank account statement and the general ledger/checkbook register. With these systems, you need to take an additional step to run a report that reflects the balances of all individual client ledgers that you will compare to the bank account statement balance and the general ledger/checkbook balance.

Choices for software packages range from the basic to the sophisticated.[2] So, what's out there? These are some of the most popular suites:

- Accounting
  - Excel, Quicken, QuickBooks.
- Billing
  - TimeSlips, Bill4Time
- Case management:
  - Clio, RocketMatter, PC Law, Amicus.

[2] This is not an exhaustive list. The State Bar does not guarantee or endorse any particular software package.

Excel is not legal-specific. This programs is *free* if you own the Microsoft Office Suite. It is are relatively easy to learn for basic trust account management purposes. It is good for lawyers not needing to integrate the trust accounting function with time and billing or other practice management software. This is good for firms with 10 clients or fewer with limited activity. Free spreadsheet-style ledger templates are available from the State Bar of Arizona.

A sole practitioner or small firm with few transactions may find a simple, inexpensive program that functions basically, like a checkbook to be satisfactory for maintaining the trust account. Quicken, for example, will not only do the math to provide a running balance for the entire account, but can be set up to provide the equivalent of an individual client ledger by using the client name in the "category," field. The lawyer can then sort by "category" and get a display on the screen or a print-out of all deposits and disbursements related to that client, including a running balance.

Quicken is one example of a single entry bookkeeping program. In a single entry system, only one entry is made for any given transaction. For example, when a check is written in Quicken, the lawyer simply enters the amount of the check and the computer deducts it from the balance. Although the lawyer must designate the client in "category" if he or she wants to use the computer to create client ledger equivalents, there is no need to enter both debits and credits.

Quicken is user-friendly and easy to learn. Quicken has limited automated functions for the trust account, but can be customized to accommodate a law firm trust account. The system must be set up to show running balances on all ledger reports, which can be difficult to do. Quicken can print checks and the Home and Business version is capable of limited invoicing.

In a double-entry system, however, there must be at least one debit and at least one credit for each transaction, with the total dollar amount recorded as debits always equal to the total amount recorded as credits. An examples of double-entry bookkeeping system is QuickBooks.

QuickBooks Pro/Premier have more features for law firms, yet it is not legal-specific. It now has Legal Wizard to guide you through the installation, and will set up reimbursable cost accounts, (i.e. copies, postage). The software links to Amicus Attorney, Time Matters, Practice Master, and more. With the Case Management program link, it provides a fully integrated accounting function. To access the Lawyer's Guide to Setting up a Trust Account Using QuickBooks, go to www2.mnbar.org/qbguide/qbguide7.htm or take a look at **Maintaining a Trust Account Using QuickBooks**, by Dianne Lynette Benton.

TimeSlips (by Sage) has a trust account capability integrated with time and billing functions (client ledgers only). It is not legal-specific, but many solo practitioners and small law firms use it. TimeSlips links with Amicus Attorney, Time Matters, Abacus Law, and other case management programs. You can purchase an extra module for handling a

general account. Remember, however, that TimeSlips must be set up so that a running balance after each transaction is included on all ledgers.

Bill4Time (cloud based) has time and billing features. It generates client ledger reports and a general ledger report, but these alone are not sufficient for maintaining your trust account; Bill4Time does not provide a reconciliation with the bank statement. The program links to QuickBooks, but it cannot print checks.

Clio (cloud software) had time and billing features. It maintains client trust balances and uses a simple ledger; however, it can be hard to get a proper general ledger. You will need to conduct your own 3 way reconciliation. It links to QuickBooks, but it is not yet available for QuickBooks Online version.

RocketMatter (cloud software) has time and billing features. It will generate a client ledger report (but you need to add the payor and check #s). A general ledger report is available. You will need to conduct your own 3 way reconciliation because it doesn't reconcile to the bank statement. It cannot print checks, but it does link to QuickBooks.

PCLaw is a legal-specific program that provides fully integrated trust accounting, time and billing features, and general ledger accounting. The Pro Version includes calendaring, document management, and case management functions. Modules are also available for remote computing. The program can also print checks and e-mail invoices.

Amicus Accounting is legal-specific. The program has fully integrated trust accounting, time and billing features and general ledger accounting functionality. It offers a seamless integration with front office and case management functions (Amicus Attorney Small Firm). It can be purchased as a stand-alone program, and it prints checks as well.

Amicus Premium Billing is legal-specific. The program has fully integrated trust accounting, time and billing features, but not general ledger. An optional module with full front office and case management functions (Amicus Premium) is available. The program is not available as a stand-alone. It can also print checks.

One of the practical differences between general business and law-specific accounting software is that law-specific programs are built around the concept that each client's money in a trust account has to be accounted for separately from every other client's money. Therefore, when an entry is made in the trust account for a disbursement, the software prompts the user to enter the name of the clients and automatically performs a check to assure that that particular client has adequate funds to cover the disbursement. Once the transaction is made, the software automatically updates that client's ledger as well as the overall account records.

By contrast, in a program not designed specifically for legal use, there is no automatic check of the total for the individual client, and the computer user must take steps (such as sorting the general ledger/checkbook register by category) to determine whether the

particular client has sufficient funds.

Some lawyers don't want to change the product they currently use for timekeeping and billing, but want to link to a program that supplements their system with the ability to maintain records on both the trust and operating accounts. An example of this combination is TimeSlips, which, although it was not specifically designed for lawyers, is widely used in the legal environment for timekeeping and billing. Another example is Quicken.

Using a computerized program for maintaining the trust account reduces the risk of mathematical error and provides the capability to sort data to instantaneously acquire information about a client's funds on the screen. However, all computer programs still require human input of data, and, while the risk of human error can be reduced by decreasing the need for multiple entries of the same data, the risk of human error cannot be totally eliminated through technology. Therefore, the lawyer, who is the person most familiar with the client's matter and the one most likely to recognize if an error has occurred, must still be vigilant in assuring that the client's money is properly protected and accounted for until its final disbursement.

H. What records do YOU have to keep of other properties?

You have a responsibility to protect and keep track of any client property, even if it is not money. It is important that at any point in time you know what property you are holding, when it was received and where it is located. For example, if you are holding securities for a client they should be kept in a secured place such as a safe deposit box and you should have a log showing when you received the securities, which bank they are located at, and if returned to the client, the date you returned them.

I. Other Resources

- Go to the vendor website.
- Read features, versions, and hardware requirements.
- Read compatibility with other software (Palm software, time & billing, accounting)
- Training and/or manuals provided.

J. Reminders

- After each transaction, calculate and record a new running balance of the total in the account on the general ledger/checkbook register, as well as a running balance on the respective individual ledger for the client on whose behalf the transaction was made.

- Each month, perform a three-way reconciliation: Calculate the total for all individual client ledgers, compare that to the total in the general ledger/checkbook register (if it doesn't match, find the discrepancy before proceeding), then reconcile your general ledger/checkbook register to the bank statement, adjusting for outstanding checks, deposits in transit (made after your bank's cut-off for that month's bank statement), and any bank charges.

- Remember that trust account records, including bank statements, canceled checks, duplicate deposit slips, client ledgers and reports to clients accounting for their funds, must be maintained for a minimum of five years following termination of representation of that specific client.

- ALL transactions must be recorded to a ledger.

- Total of the ledgers should always match the balance in the general ledger/checkbook register.

SECTION IX: RECONCILIATION

"Reconciliation" means checking the three basic records you are required to keep - the bank statements, the client ledgers, and the general ledger/checkbook register - against each other so you can find and correct any mistakes.

Rule 43(b)(2)(C) requires you to reconcile your client trust account records because mistakes are bound to happen when people keep track of money. Even banks make mistakes when it comes to recording money transactions. That's because when you're working with numbers, mistakes are easy to make and difficult to notice. No amount of training can completely eliminate these mistakes.

To make sure that you find and correct these mistakes, record every client trust account transaction twice (on your client ledger and your general ledger/checkbook register), and check these records against each other and against the bank's records. For example, let's say you deposit a check for $1,000 into your client trust account but mistakenly record it as "$10,000" in your client ledger and add $10,000 to your client's running balance. In your general ledger/checkbook register, you recorded the check correctly and added $1,000 to your client trust account's running balance. How will you find the mistake? The general ledger/checkbook register balance is right, so you won't find the mistake by bouncing a check. The numbers in the client ledger all add up so there's no way to tell you made a mistake. Unless you compare your client ledger balance to your general ledger/checkbook register balance, you won't be able to find the recording error. And unless you compare your client ledger and general ledger/checkbook register against the bank statement, you won't know which entry was right - $10,000 or $1,000.

We've just described the reconciliation process. The theory is that it's unlikely that the same mistakes will be made in three different records - the client ledgers, the general ledger/checkbook register and the bank statement - so if those records are all checked against each other, any mistakes will show up.

Rule 43(b)(2)(C) requires that your client trust account records be reconciled **every** month. While you are not required to keep a written record of your "monthly three-way reconciliation" of your client ledgers, general ledger/checkbook register and bank statements, it is always a good idea to do so because it shows you went through the reconciliation process. It's fine to hire a bookkeeper or the equivalent, but you are still personally responsible for accounting to your clients and to the State Bar for the money in your client trust accounts. Therefore, even if you never intend to do the reconciling, you should understand the process. Even if it's your bookkeeper's mistake, if you bounce a client trust account check, you're the one your client or the State Bar is going to come to for an explanation.

You can't do a reconciliation for one month until you're sure you have correct balances in all your client ledgers and general ledger/checkbook register for the previous month. If

you haven't recently reconciled your books, or if you are worried that they're wrong, you may want to bring in a bookkeeper to straighten them out before you take on the monthly reconciliations yourself.

Once you have correct balances for the previous month, you are ready to reconcile.

There are four main steps in reconciling your books (See Pages 80-83.):

1. Reconciling the general ledger/checkbook register with the client ledgers to make sure they agree with one another.

2. Entering bank charges and interest shown on the bank statement into your general ledger/checkbook register and client ledgers as appropriate.

3. Reconciling the general ledger/checkbook register and client ledgers with the bank statement to make sure that your records agree with the bank's.

4. Entering corrected month ending balances and corrected current running balances into your general ledger/checkbook register and client ledgers.

As you can see, the third step of the reconciliation process is comparing your monthly bank statement with the account records you've created. A bank statement is a list of all the withdrawals, deposits, charges and interest that the bank has credited to your account during the month. For IOLTA accounts, the bank statement may also show interest paid to the State Bar. It takes some banks several weeks to prepare and mail out statements for the previous month; that means you may be reconciling your books as much as three or four weeks after the month you are reconciling. Also, it can take days or weeks for checks to be presented for payment. These delays mean that you can't just compare the balance in your general ledger/checkbook register to the balance shown on the bank statement to see if anything is wrong. You have to "adjust" your account balance by backing out all the transactions that weren't debited or credited by the time the bank statement was prepared.

The goal of the reconciliation process is to figure out the corrected month ending balance for the month you are reconciling (that is, the amount of money that was actually in the account on the last day of the month) and the corrected current running balance as of the date you complete the reconciliation (that is, the amount of money that is actually in the account now) by entering interest, bank charges and mistake corrections into your general ledger/checkbook register and client ledgers. (You'll put these entries in the space you left after the last entry of the month so that you could add entries during the reconciliation process.) Since you can't be sure you've found every mistake until you've finished reconciling, you can't enter a corrected month ending balance or a corrected current running balance into your general ledger/checkbook register and client ledgers until you've finished the reconciliation process.

Remember that a three-way reconciliation should be conducted **every month** for **every** client trust account.

When completing the three-way reconciliation, it's a good idea to use an adding machine or other calculator that will produce a printed record of the calculation you performed. That way, if your records don't match, you can easily check to see if the reason is a mathematical mistake made while preparing the form.

These are the client ledgers that will be used for the three-way reconciliation example:

Client: Alpha, A.				Matter: 111111		
R	**Number**	**Date**	**Description of Transaction (Payor/Payee)**	**Payment**	**Deposit**	**Balance**
	Deposit	12/15/2016	Deposit Alpha – fees		$250	$250
	1001	01/17/2017	Dee Fender, Esq. – earned fees	$250		$0

***** ***** ***** ***** ***** ***** *****

Client: Beta, B. - FEES				Matter: 222222		
R	**Number**	**Date**	**Description of Transaction (Payor/Payee)**	**Payment**	**Deposit**	**Balance**
	Deposit	02/01/2017	Deposit Beta - $1,500 fees and costs		$1,500	$1,500
	1002	02/15/2017	Superior Court – Nowhere County Filing Fee – cost	$125		$1,375
	1003	02/15/2017	Nowhere Vital Records – Birth Cert. – cost	$75		$1,300
	1004	03/19/2017	Dee Fender, Esq. – earned fees	$600		$700
	1005	04/19/2017	Dee Fender, Esq. – earned fees	$400		$300

***** ***** ***** ***** ***** ***** *****

Client: Gamma, G. – FEES				Matter: 333333		
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	05/02/2017	Deposit Gamma - $1,200 fees (earned upon receipt)		$1,200	$1,200
	1007	05/16/2017	Dee Fender, Esq. – earned fees	$1,200		$0
Client: Gamma, G. – COSTS				Matter: 333333		
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	05/02/2017	Deposit Gamma - $250 costs		$250	$250
	1006	05/16/2017	Record Round Up - costs	$150		$100

***** ***** ***** ***** ***** ***** *****

Client: Delta, D.				Matter: 444444		
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	06/03/2017	Deposit Delta - $15,000 fees (unearned)		$15,000	$15,000
	1008	06/17/2017	Dee Fender, Esq. – earned fees 8 hrs @ $250/hr	$2,000		$13,000
	1009	06/17/2017	D. Delta – refund	$13,000		$0

***** ***** ***** ***** ***** ***** *****

Client: Epsilon, E.				Matter: 555555		
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	07/15/2017	Deposit Epsilon - $2,000 fees (unearned)		$2,000	$2,000
	Returned Deposit	07/18/2017	Epsilon Returned deposited check for insufficient funds	$2,000		$0
	Deposit	07/31/2017	Deposit Epsilon - $2,000 fees (unearned)		$2,000	$2,000

***** ***** ***** ***** ***** ***** *****

Client: Administrative Funds, Dee Fender, Esq.				Matter: 999999		
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	12/01/2016	Deposit to open account – Fender		$50	$50
	Bank Fee	07/18/2017	Client Epsilon Returned Deposit Fee	$5		$45
	Deposit	07/31/2017	Client Epsilon reimbursement for $5 returned deposit bank charge		$5	$50

This is the general ledger/checkbook register that will be used for the three-way reconciliation example:

General Ledger/Checkbook Register						
R	Number	Date	Description of Transaction (Payor/Payee)	Payment	Deposit	Balance
	Deposit	12/01/2016	Deposit to open account – Fender		$50	$50
	Deposit	12/15/2016	Deposit – Alpha fees		$250	$300
	1001	01/17/2017	Dee Fender, Esq. – Alpha earned fees	$250		$50
	Deposit	02/01/2017	Deposit – Beta $1,500 fees and costs		$1,500	$1,550
	1002	02/15/2017	Superior Court – Nowhere County Filing Fee – Beta cost	$125		$1,425
	1003	02/15/2017	Nowhere Vital Records – Birth Cert. – Beta cost	$75		$1,350

	1004	03/19/2017	Dee Fender, Esq. – Beta earned fees	$600		$750
	1005	04/19/2017	Dee Fender, Esq. – Beta earned fees	$400		$350
	Deposit	05/02/2017	Deposit – Gamma $1,200 fees (earned upon receipt) $250 costs		$1,450	$1,800
	1006	05/16/2017	Record Round Up – Gamma costs	$150		$1,650
	1007	05/16/2017	Dee Fender, Esq. – Gamma earned fees	$1,200		$450
	Deposit	06/03/2017	Deposit – Delta $15,000 fees (unearned)		$15,000	$15,450
	1008	06/17/2017	Dee Fender, Esq. – Delta earned fees 8 hrs @ $250/hr	$2,000		$13,450
	1009	06/17/2017	D. Delta – refund of unused advanced fee	$13,000		$450
	Deposit	07/15/2017	Deposit – Epsilon $2,000 fees (unearned)		$2,000	$2,450
	Returned Deposit	07/18/2017	Epsilon - returned deposited check for insufficient funds	$2,000		$450
	Bank Fee	07/18/2017	Epsilon Returned Deposit Fee	$5		$445
	Deposit	07/31/2017	Deposit – Epsilon $2,000 fees (unearned) with reimbursement for $5 returned deposit bank charge		$2,005	$2,450

This is the trust account bank statement that will be used for the three-way reconciliation example:

Bank of Wegottayourmoney

Dee Fender, Esq.
Arizona Bar Foundation Trust
1201 E. Easy Street, Suite #100
Sunnyvale, AZ 85898

Account Number: 000200800888
Activity Through: 12/01/2012 – 07/31/2013

Beginning Balance	12/01/2016	$50.00
Ending Balance	**07/31/2017**	**$520.00**

Deposits/Credits

Date	Dollar Amount	Type
12/01/16	$50.00	Deposit
12/15/16	$250.00	Deposit
02/01/17	$1,500.00	Deposit
05/02/17	$1,450.00	Deposit
06/03/17	$15,000.00	Deposit
07/15/17	$2,000.00	Deposit

Total Deposits/Credits $20,250.00

Withdrawals/Debits

Check #	Dollar Amount	Date
1001	$250.00	01/17/17
1002	$125.00	02/15/17
1004*	$600.00	03/19/17
1005	$400.00	04/19/17
1006	$150.00	05/16/17
1007	$1,200.00	05/16/17
1008	$2,000.00	06/17/17
1009	$13,000.00	06/17/17

*Indicates preceding check (or checks) is outstanding.

Other Withdrawals/Debits

Type	Dollar Amount	Date
Returned Deposit 07/15/17	$2,000.00	07/18/17
Returned Deposit Fee	$5.00	07/18/17

Total Withdrawals/Debits $19,730.00

Daily Balance

12/01/16	$50.00	03/19/17	$825.00	06/17/17	$525.00
12/15/16	$300.00	04/19/17	$425.00	07/15/17	$2,525.00
01/17/17	$50.00	05/02/17	$1,875.00	07/18/17	$520.00
02/01/17	$1,550.00	05/16/17	$525.00	07/31/17	$520.00
02/15/17	$1,350.00	06/03/17	$15,525.00		

THREE-WAY RECONCILIATION SHEET

Step 1: Total Client Ledger Balances:

1)	Administrative Funds	$50
	Client Name	**Ledger Balance**
2)	Alpha	$0
	Client Name	**Ledger Balance**
3)	Beta	$300
	Client Name	**Ledger Balance**
4)	Gamma	$100
	Client Name	**Ledger Balance**
5)	Delta	$0
	Client Name	**Ledger Balance**
6)	Epsilon	$2,000
	Client Name	**Ledger Balance**

Total of Client Ledger Balances as of, 07/31/2017..... **$2,450**

Step 2: Enter General ledger/checkbook register Balance as of, 07/31/2017..... **$2,450**

Step 3: Enter Ending Balance per bank statement, 07/31/2017..... **$520**

Step 4: Enter total outstanding deposits..... **$2,005**
(Deposits made to the account, yet not captured on bank statement. These will be ADDED to the bank statement amount.)

Step 5: Enter total outstanding checks..... **$75**
(Checks that have been drawn from the account, yet not captured on bank statement. These will be SUBTRACTED from the bank statement amount.)

Step 6: Bank Service Charges/Interest (-/+)..... **$0.00**
(ADD any interest (non-IOLTA) as reflected on bank statement. SUBTRACT any bank fees.)
Make sure that these transactions are reflected on the proper individual client ledger(s) and general ledger/checkbook register.

Step 7: Calculate Adjusted Balance..... **$2,450**
(Ending bank statement balance plus outstanding deposits minus outstanding checks, plus interest, minus service charges.)

Reconciliation: All three should match…

Total of all client ledgers..... **$2,450**
(Total from Step 1.)

Adjusted Bank Balance..... **$2,450**
(Total from Step 7.)

General ledger/checkbook register Balance..... **$2,450**
(Total from Step 2.)

A. Reconcile the General Ledger/Checkbook Register With the Client Ledgers

For illustrative purposes only, the bank statement provided for this reconciliation covers the period of 12/01/2016 through 07/31/2017. In every day practice, your trust account bank statement would only cover one month, e.g., 07/01/2017 through 07/31/2017.

The first part of reconciliation is to reconcile the general ledger/checkbook register with the client ledgers. The purpose of this step is to make sure that the entries in your client ledgers agree with the entries in your general ledger/checkbook register.

On Page 79, **in Step 1**, on the lines above "Client Name," write the name of each client whose money you are holding in the client trust account. On the lines above "Ledger Balance," write the running balance as of the last day covered by the bank statement (in this case, July 31, 2017) from each client ledger next to the name of that client. (For your common client trust account, this may require more lines than shown here. For an individual client trust account, you will only need the first line.) Add up the client ledger balances in the "Ledger Balance" column and write in the total after "Total of Client Ledger Balances as of, 07/31/2017." Even if only one client's money is in the client trust account, you have to write that client's balance on this line.

In Step 2: Notice that the "Total of Client Ledger Balances as of, 07/31/2017" exactly matches the "General ledger/checkbook register Balance." That means that your individual client ledger balance entries for the month agrees with your general ledger/checkbook register entries, and you're ready to move on to the next step of the reconciliation process.

When the "Total of Client Ledger Balances" *doesn't* exactly match the "General Ledger/Checkbook Register Balance," don't panic; you've found a mistake, and that's what **reconciliation** is for. You can call in a bookkeeper to help you, or make the correction yourself. Since you record every deposit and withdrawal twice, if you systematically compare each entry in the general ledger/checkbook register with the corresponding entry in the client ledger, and check the new balance you entered after each entry, you will always find the mistake.

When you've found and corrected the mistake, move on to Step 3.

B. Reconcile the General Ledger/Checkbook Register with the Bank Statement

Step 3: In the space after, "Ending Balance per bank statement, 07/31/2017," write in the running balance for the client trust account as of the last day covered by the bank statement.

Steps 4 and 5: The purpose of this step is to make sure that the bank's records of the deposits and withdrawals you've made to your client trust account during the past month match your records. Since you've already reconciled the client ledgers with the general ledger/checkbook register, you know that the entries in the client ledger agree with the ones in the general ledger/checkbook register. Therefore, unless you find a mistake during this stage of the reconciliation process you only have to compare the bank statement with the general ledger/checkbook register.

Deposits and withdrawals not posted on bank statement. Generally, the bank sends out statements one to three weeks after the end of the month. As a result, by the time you reconcile the account, you will usually have made deposits or withdrawals that aren't shown on the bank statement. In addition, checks you wrote or deposits you made may not have cleared by the time the bank produced the statement, and therefore the amounts of those checks or deposits won't be reflected in the account balance shown on the bank statement. Thus, in order to compare the balance the bank statement says is in the account at the end of the month with the balance your general ledger/checkbook register shows for the end of the month, you have to adjust the general ledger/checkbook register balance by ***adding*** all un-credited deposits and ***subtracting*** all un-debited withdrawals.

To find out which transactions haven't been posted, you have to compare the entries on the bank statement with the entries in your general ledger/checkbook register.

Go through each entry on the bank statement and compare it to the corresponding entry in your general ledger/checkbook register. If the entry in the general ledger/checkbook register exactly matches the entry on the bank statement, mark off the entry in the general ledger/checkbook register to show that the money has cleared the banking process, and mark off the entry on the bank statement to show that you have verified it against the general ledger/checkbook register. The marks in the general ledger/checkbook register will help you keep track of items like checks that are never cashed, which otherwise can become those small, inactive balances that make your account harder to reconcile. The marks should be permanent (i.e. in ink) and clearly visible, but shouldn't make it harder to read the entries. You should use the same mark consistently, to avoid confusion later.

When you are finished, all the entries on the bank statement should be checked off to show that you have verified them against the corresponding entries in the general ledger/checkbook register. Now go back through the general ledger/checkbook register to find any entries that are unmarked; these transactions haven't yet been debited or credited by the bank.

As you go through the bank statement, there are two kinds of mistakes you may find:

1. **You find a deposit or withdrawal listed on the bank statement that isn't in your general ledger/checkbook register.** To correct this mistake, go through your canceled checks (if it's a withdrawal) or deposit slips (if it's a deposit) until you find the one that reflects the transaction on the bank statement. If you can't find a

canceled check or deposit slip that matches the entry on the bank statement, contact your banker and ask him or her to help you track down the transaction. DON'T record the bank statement entry in your records until you verify that the transaction occurred; banks make mistakes too.

2. **An entry in the bank statement is different from the corresponding entry in the general ledger/checkbook register.** You correct this mistake the same way you correct a transaction you forgot to record. First, find the canceled check or deposit slip that shows the transaction to figure out which record is correct, the general ledger/checkbook register or the bank statement. If you can't find a canceled check or deposit slip for this transaction, contact your banker and ask him or her to help you track it down before you make any changes in your records.

If the canceled check or deposit slip shows that the bank statement is wrong, write a note on the bank statement that clearly describes the mistake, then contact your banker and tell him or her to correct their records. If it shows that your general ledger/checkbook register is wrong, record the correction in the general ledger/checkbook register *and* the appropriate client ledgers. These must be entered twice in both the general ledger/checkbook register and the client ledger for the client on whose behalf you deposited or paid out the money.

Step 6: Make sure that bank charges and interest credits reflected on the bank statement are also reflected in your records. Since you may not know what these bank charges or interest credits are until you receive the bank statement, you need to enter them into your records after you receive the bank statement.

All bank charges must be recorded in the general ledger/checkbook register. If a bank charge was incurred on behalf of a specific client (as for example, a charge for wiring money to a client), the charge must also be entered on that client's client ledger. (This ensures that the general ledger/checkbook register balance will continue to match the total of the individual client ledger balances.) If the charge was not for a specific client (for example, a charge for printing common client trust account checks), the charge must also be entered in the Administrative Funds/Bank Charges ledger.

The next step is to reconcile the balance the bank statement shows for the end of the month you are reconciling with the balance your general ledger/checkbook register shows for the date.

C. Calculate the Adjusted Balance

Step 7: In the space after "Calculate Adjusted Balance," write the balance **after** you calculate the following:

1. Ending Bank Statement Balance
2. Plus All Outstanding Deposit Amounts
3. Minus All Outstanding Check Amounts
4. Plus Non-IOLTA Interest
5. Minus Bank Fees and Charges

D. Trust Reconciliation Sheet

The total from Step 1, Total of all client ledgers, Step 2, General ledger/checkbook register, and Step 7 Adjusted Bank Balance, should all match. If they do, you have successfully reconciled the account. If it doesn't, call in a bookkeeper or go back and recheck your ledgers and bank statement to find and correct the mistake(s).

Now clip all the pages that relate to the reconciliation process together (and any adding machine tapes) and file them away.

SECTION X: INTERNAL CONTROLS

A. The Need for Control

Having a good working set of accounting records is an essential step toward the sensible management of client trust funds. It is also the first essential to avoiding theft. However, it is only a first step. Without required records, the lawyer has not met the obligation to clients or to the Court. Moreover, the lawyer without proper records can be responsible for knowingly, or negligently invading clients' trust funds. Equally important is the fact that the lawyer who has poor records is ripe for theft by partners, associates, bookkeepers, and secretarial employees.

Even when records are properly established, however, records alone do not satisfy the lawyer's ethical obligations and do not serve as a defense against theft by others. In order to meet these challenges, one must: (a) maintain records in proper working order; and (b) exercise control over these records by actively reviewing them in accordance with a regular oversight program. This chapter outlines some of the steps by which lawyers can control their client trust account and meet ethical obligations and minimize the possibilities of theft.

B. Diversification of Financial Functions

The cardinal rule in avoiding theft is to divide the monetary functions in a law office. This is particularly difficult for a small firm or sole practitioner. However, if one secretary, for example, is given authority and responsibility to handle the trust and business accounts, reconcile these accounts, handle bank statements and, occasionally, even sign checks, that one person can easily doctor the records to cover up a theft and avoid detection for a long period of time. The same is true where one lawyer in a firm has sole responsibility for accounts with no oversight. Either one could unilaterally steal the law firm blind.

Ideally, functions can be divided this way:

- Only a lawyer may sign trust account checks.

- Only one secretary or bookkeeper should have access to trust and business accounts records. Access by many secretaries makes it more difficult to pinpoint responsibility and increases opportunities for theft.

- A separate staffer should open all mail and record all incoming checks, which

should then be given to the secretary/bookkeeper responsible for maintaining the accounts.

- All accounting records should be reconciled by the lawyer or by an independent accountant or bookkeeper on a monthly basis.
- The lawyer responsible should receive directly all monthly bank statement unopened or directly by electronic transmission.

- An annual (or quarterly) audit should be done by an outside accountant.

This layered diversification of responsibility minimizes the opportunities for fraud, since successful theft in this system requires collusion between two or more persons.

C. Exercising Control of Records

Control is not a self-executing concept. It must be exercised. The following are positive steps that can be taken to exercise control over trust and business accounts funds:

1. When the lawyer signs trust account checks, a review of the client's ledger should be made to determine the validity of the checks drawn.
2. A periodic review should be made of the reconciliation book prepared by the secretary/bookkeeper to determine its correctness.
3. A perusal and inquiry of checks outstanding for an extended period of time should also be made periodically.
4. Randomly, a review of the current balance on the general ledger/checkbook register and the balance of funds reflected on the client's ledger should be undertaken when a disbursement is made to ensure that there are sufficient collected funds to accommodate the disbursement.
5. The bank statement (with canceled checks) should be delivered unopened to the lawyer or directly by electronic transmission. The lawyer should then peruse the canceled checks for the following:

    a. Are the payees familiar?
    b. Are the clients who are named on the checks firm clients?
    c. Are endorsements made by the payee or by an employee in the law office?
    d. Are checks being cashed instead of being deposited? If so, communicate with one or two payees to make sure they received the money?
    e. Are duplicate payments being made? If so, is one legitimate and the other being taken by an employee?
    f. Is your signature on all checks authentic? DO NOT use signature stamps.

6. Randomly review bank statements that are delivered to you unopened to make sure that none are missing. Personally obtain and review any missing bank statements and also any checks that have been outstanding for a long time or which are missing.

D. Exercising Control Over Employees

1. Hiring

Just as a dispossess action is no substitute for finding a good tenant, so too a lawsuit or criminal action is not much solace for hiring a dishonest employee. There is no substitute for hiring good, honest employees. While there are no guarantees on new employees, there are basic steps that should be taken. It is most important to do a thorough background review and to check references.

One law firm hired a bright, attractive secretary who had excellent skills. They later fired her for stealing $26,000 and only then inquired of her former employer to find out she had previously been fired from that firm and criminally prosecuted for theft.

2. Instruction

Lawyers are ethically obligated under Rule 43(b)(1)(B) to properly instruct and oversee employees to ensure that their actions are compatible with the lawyer's professional obligations. This is particularly true of those employees who will be involved with the handling of clients' and firm funds. Give them a copy of the Rules and this manual and make sure they understand the basics. Then follow up periodically and check their compliance.

3. Supervision

Sometimes employees seem too good to be true. Consider these signs carefully if you believe there could be theft or fraud by an employee:

- Does the employee come in early (usually before the boss) and stay later than necessary (usually after the boss has left)?

- Does the employee come in on Saturdays, Sundays and holidays when not required to do so?

- Does the employee fail to take earned vacations?

E. Process

It is essential that all law firms develop a sound, routine process for handling checks that any deviations will serve to highlight questionable practices. Key among these processes are:

- Use restrictive endorsements on all checks received, marked "for deposit only" into a specific account or accounts.
- Require two signatures for large checks.
- Never use a facsimile signature stamp.
- Never write trust account checks to cash.
- Never use an ATM card to withdraw trust funds.

F. Billing Clients Regularly

One of the quickest ways to determine whether or not fees paid by clients for legal services (as well as other monies paid to the law firm on the client's behalf) have been handled improperly, is to bill clients promptly. If money is diverted to other purposes by law firm staff and is not correctly reflected on the bill, the client will be the first to complain. For this reason, many lawyers also account to clients more frequently than they are otherwise obligated to do.

G. Separate Trust Accounts For Lawyers in Same Firm

There is no limit to the number of client trust accounts that may be maintained by a lawyer or law firm. There is also nothing that prohibits each lawyer in a firm from maintaining trust accounts in the lawyer's own name separate from the firm. However, for good control, oversight and accountability, firm accounts are preferable to individual accounts. When individual partners or shareholders have separate trust accounts, they unnecessarily expose other principals to liability, usually without the other principals having any ability to exercise oversight or control over the handling of clients' funds in the separate accounts.

H. Insurance—The Ultimate Control

The ultimate risk control mechanism is insurance. Despite all prudent audit control steps one may take, it is still possible that a theft may occur. If reasonable audit control steps have been followed, however, such a theft will be detected at an early time and, hopefully, while the amount of money taken is small. Nevertheless, in a time where typical mortgage

amounts run from $100,000 to $400,000, just one theft can expose the lawyer to tremendous financial risk.

Insurance may be the key to avoiding liability for theft by another lawyer or employee in the firm. Malpractice insurance policies usually have a standard exclusion relating to criminal, fraudulent and dishonest conduct of an insured. However, many also contain an "Innocent Insured Exception" to this inclusion. Some companies writing lawyer malpractice policies have a standard provision in its "claims made" policy that, in effect, covers each and every insured who did not personally commit, participate or acquiesce in the criminal, dishonest, fraudulent or malicious act, or remain passive after having personal knowledge of such act.

Under this policy an "innocent" lawyer partner, shareholder or sole practitioner would not be faced with declaring personal bankruptcy if another lawyer in the firm stole $800,000 as the result of a gambling, drug or alcohol problem. Every lawyer should inquire into the feasibility of having the firm's malpractice policy contain this "innocent" lawyer exception. Lawyers should also inquire about the cost of "Dishonest Employee" coverage for non-lawyer staff members who handle trust and business funds.

SECTION XI: RANDOM TRUST ACCOUNT EXAMINATIONS

Guidelines have not yet been developed by the Board of Governors. Until the guidelines have been established, there will be no random trust account examinations.

SECTION XII: OTHER RELEVANT TRUST ACCOUNT TOPICS

A. Abandoned Property/Funds

Three situations provide unsolvable problems for lawyers:

- Missing Owners—cases in which lawyers know to whom trust funds belong, but owners cannot be found;

- Unclaimed Trust Funds—cases in which lawyers know to whom trust funds belong, but the owners fail or refuse to claim them; and

- Unidentifiable Trust Funds—cases in which the ownership of trust funds has become impossible to determine due to the passage of time (e.g. the merging of firms).

Maintenance of these funds, like all small inactive balances, hinders the process, since these odd amounts of funds must be carried from month to month. Ethics Opinion 97-03 provides a procedure for disposing of these funds. In order to do so, funds must be unidentified or unclaimed, or the owners must be missing, for over three years. The lawyer must then make a "reasonable" search to ascertain the facts. If the funds remain unidentified or unclaimed, or if the missing client cannot be found or will not accept the funds, the lawyer, at the end of the three years, should forward the funds according to the Arizona Revised Unclaimed Property Act Title 44, Chapter 3, Article 1. Also see Arizona Department of Revenue Publication 651.

There are several ways to address the problem of trust account checks that are not cashed for a significant period of time. Some lawyers print "Void After 90 Days," on trust account checks to persuade payees not to hold the checks. The notation does not guarantee that the bank will not honor the check after 90 days. This issue should be addressed with the bank in advance. Other lawyers contact all recalcitrant payees who fail to negotiate a trust account check after a certain period of time (usually six to nine months). Certified mail should be used if warranted by the amount of the check. If the payee cannot be located or a reply is not received within a reasonable amount of time, a stop payment should be placed on the check. If a stop payment order is placed on a check, the check may still be cashed. The bank's procedures for stop payment orders should be understood in advance. After payment is stopped on a check, the funds are noted as returned on the individual client ledger. If the lawyer believes the funds have been abandoned, the lawyer must follow the Arizona escheat requirements.

B. Trust Account Overdraft Notification

All financial institutions, approved as depositories for client trust accounts, are required as a condition of such approval, to report to the State Bar of Arizona chief bar counsel in the event any properly payable client trust account instrument is presented against insufficient funds, regardless whether the instrument was honored. Rule 43(f)(3)(D).

The primary purpose of overdraft notification is to detect serious trust account violations. It should be recognized that the creation of an overdraft, if adequately explained, does not per se indicate a misappropriation of clients' trust funds. Overdrafts can arise from a number of causes, such as a bank encoding error or the failure to timely credit a deposit to the trust account. The purpose of the overdraft notification procedure is, through documentation, to differentiate these situations from a situation where a lawyer is misappropriating client's trust funds.

Normal banking practice requires the financial institution to give notice to the lawyer simultaneously with the notice of overdraft to the State Bar chief bar counsel. Where there is no impropriety, the lawyer will be as interested as anyone in finding the cause for the overdraft as quickly as possible.

On receipt of the overdraft notice, a trust account examiner will communicate in writing with the lawyer or law firm, requesting a written, documented response that explains the overdraft within 20 business days of the lawyer's receipt of that letter. In many instances, the lawyer will already have communicated with the financial institution and will have determined and corrected the error resulting in the overdraft.

The initial inquiry by the trust account examiner is a disciplinary request and, in accordance with court rules, a written response by the lawyer is required. A failure to respond is serious and will potentially result in a motion for the lawyer's temporary suspension. Most overdraft notices are handled by responses from the lawyer properly documenting the cause of the overdraft. If further information is necessary to supplement the lawyer's initial response, it will be requested.

One of the most frequent causes of overdrafts relates to a failure to **timely** deposit trust monies. Checks drawn against uncollected funds will cause an overdraft to be reported. However, if a deposit is not made so that the seller or realtor for example, presents a closing check, in a real estate matter, on a banking day prior to the deposit (assuming there are no other trust funds in the account), an overdraft has to occur. Several things can (and should) be done to prevent these overdrafts:

- deposit funds promptly so they are credited promptly, and
- do not issue a trust account check or make an electronic disbursement until you are sure the funds are collected, and

- if it is a limited risk deposit, make sure you have other funds available in case the check is the deposit fails.

Some lawyers do not immediately reimburse the trust account when they discover the account was overdrawn due to an accounting error or when a deposited check is returned for insufficient funds. When such an inadvertent debit to the account is discovered, the lawyer is responsible for reimbursing the account. Reimbursement of the trust account should NOT be held in abeyance pending resolution of the error (e.g., by locating the party responsible for a bad check). Any delay in reimbursing the account may result in the use of other client funds to cover the shortage, which is not permitted (conversion).

C. Closing a Client Trust Bank Account

When you need to close your trust account for any reason, here are some tips to remember:

- Be sure that the account is reconciled such that all funds remaining correspond to specific clients and/or administrative funds.

- Check with you bank to determine whether there are any charges associated with closing the account. If there will be a fee, make sure that you have enough administrative funds on deposit in the account to cover the fee.

- Do not close the account until all outstanding checks have cleared.

- Shred the checkbook and deposit slips for the account once it is closed so that these documents will not be accidentally used in the future.

- Refer to Arizona *Ethics Op. 97-03* if there is an amount of funds left in the trust account that you are unable to identify or if you are unable to locate a client.

- Refer to IRS Publication 651 regarding abandoned property.

- If you are closing the trust account to move it to a new banking institution, check to be sure that your new banking institution is qualified to offer IOLTA accounts, by going to http://www.azflse.org/azflse/IOLTA/allbanks.cfm.

- If you are closing the trust account to move it to a new banking institution, be sure that your audit trail is not lost, i.e. all funds moved from the old trust account are clearly identified by client and transferred fully to the new trust account.

- Notify State Bar Member Services with the new trust account banking information by completing the Arizona IOLTA Enrollment Form.

D. Death or Disability and the Client Trust Bank Account

Resources to assist disabled lawyers or survivors of deceased lawyers are very limited. Absent a contingency plan, probate court or a special "lawyer" conservatorship may be the only other options.

Pursuant to Rule 66, Ariz. R. Sup. Ct., the State Bar or any other interested person may petition the presiding judge of a superior court to appoint [a conservator] if…no partner or other responsible successor to the practice of lawyer is known to exist, and…the lawyer is transferred to inactive status because of incapacity or disability, or disappears or dies, or where other reasons requiring protection of the public are shown.

Pursuant to Rule 67(d), Ariz. R. Sup. Ct., neither the conservator nor any partner, associate or other lawyer practicing in association with the conservator shall…make any recommendation of counsel to any client…represent such client…

Pursuant to Rule 68(a), Ariz. R. Sup. Ct., service on a bank or financial institution of a certified copy of the order of appointment of the conservator shall operate as a modification of any agreement of deposit among such bank or financial institution, the respondent and any other party to the account so as to make the conservator a necessary signatory on any professional or trustee account maintained by the respondent with such bank or financial institution.

Pursuant to Rule 68(b) and (d), Ariz. R. Sup. Ct., the conservator shall return all client funds in the custody of the [lawyer] to the clients as soon as possible, allowing for deduction of expenses or other proper charges owed by the clients to the [lawyer]. The necessary expenses and any compensation of a conservator shall, if possible, be paid by the [lawyer] or the [lawyer's] estate.

It is prudent for a lawyer to arrange for the administration of his or her client trust account in the event of the lawyer's death or disability. A prudent lawyer is well-advised to identify someone in advance of such a contingency who can assume such a responsibility, to develop a plan that covers both the contingencies of disability and death, and to incorporate plans for the administration of the client trust account into a broader plan for winding down the lawyer's affairs if either contingency occurs.

ER 1.15 requires a lawyer to safeguard client property, including client funds, "with the care required of a professional fiduciary." ER 1.15 cmt. 1; *see also* Ariz. R. Sup. Ct., Rule 43(b)(1)(standard of performance). Consistent with that obligation, it is prudent for a lawyer to develop a plan to ensure that funds in his or her client trust account are properly administered and distributed if the lawyer dies or becomes disabled. *See, e.g.*, *Ariz. Ethics Op. 04-05*; ABA Formal Op. 92-369 at 2-4 (December 7, 1992) (consistent with ERs 1.1 and 1.3, a lawyer should have a plan in place to ensure that client matters will not be neglected in the event of his or her death).

One means of achieving this objective is to arrange to have another lawyer administer the client trust account in the event of the lawyer's death or disability. As noted by the inquiring lawyer, there are a number of different ways a lawyer can consider to accomplish this: (a) entering a letter agreement with another lawyer obligating him or her to assume responsibility over the account in the event of the lawyer's death or disability; (b) pursuant to A.R.S. § 14-5501, *et seq.*, granting another lawyer a contingent power of attorney to administer the account if the lawyer becomes disabled; (c) including a provision in the lawyer's will directing the executor of the estate or some other designee to retain a lawyer to administer and distribute funds in the account; or (d) making arrangements with someone to seek the appointment of a conservator pursuant to Rule 66(a) of the Rules of the Supreme Court of Arizona if the lawyer dies or becomes disabled.

Strictly from the perspective of complying with a lawyer's ethical responsibilities, a prudent lawyer should consider the following:

First, a lawyer should choose a means that is not only legally effective, but also fair to, and expeditious for the clients who are entitled to the funds in the account. That favors identifying and reaching agreement with an identified person who is willing to assume the responsibilities of administering the trust account, and not leaving it to a court later to find a suitable candidate. The lawyer also is ethically obligated to select someone whom the lawyer reasonably believes is competent to discharge those responsibilities. *See* Ariz. Sup. Ct. R. 43(b)(1)(A)("Due professional care must be exercised in the performance of the lawyer's duties under this Rule."). Consistent with this requirement, the designee should be a lawyer because the distribution of funds in a client trust account necessarily requires an understanding of, and accountability under ER 1.15.

Second, a lawyer should plan for both death and disability. Making a provision in a will for the handling of a trust account may satisfy a lawyer's ethical obligations if he or she dies, but such provisions are useless in planning for possible disability. Similarly, granting a power of attorney to another lawyer might be an effective way to anticipate the possibility of disability, but it is an ineffective tool in planning for a lawyer's death because such a power automatically terminates upon the grantor's death.

Third, a lawyer's plans for the disposition of his or her client trust account should be made in concert with a broader plan for the disposition of the lawyer's practice in the event of his or her death or disability. Prudence dictates that arrangements should be made with another lawyer to notify clients of the lawyer's disability or death, and to review the lawyer's files for the limited purpose of determining whether any immediate action needs to be taken to protect those clients' legal interests. *See, e.g.*, ABA Formal Op. 92-369 at 4 (such arrangements do not violate ER 1.6 because they are impliedly authorized in order for the lawyer to carry out a representation).

Consistent with a lawyer's obligations under ER 1.15(a), a prudent lawyer is well advised to develop such a plan to ensure that his or her clients' interests in the account are adequately safeguarded.

E. Fraud

Out of the blue, you receive an email from the representative of a potential foreign client, maybe from China. He flatteringly tells you – in pretty decent English -- that he is looking for a trustworthy lawyer in Arizona to help his company with a collections issue. You – you! -- are the trustworthy lawyer he has found. Your charge: you would receive money from a debtor and then transfer it to the potential foreign client. You might even be paid with a percentage of the money.

Sounds promising, right? Some easy money? And tempting, because who knows where this *one* job for an international client might lead.

You send a fee agreement to the representative. He maybe sends the agreement back, signed, and tells you that it's imperative that you wire the money as soon as possible after receiving it from the debtor. You promptly receive a check from the debtor and deposit it into your trust account. Being a diligent lawyer, you confirm with your bank that the money has been credited to your account, and you wire it as directed.
And then a few days later, your bank tells you that the check wasn't legitimate. The bank has debited your trust account thousands of dollars.

You already know about the email scams in which a Nigerian government official allegedly needs your help to move money out of the country. You've probably received those emails and immediately - and rightly - disregarded them because they look so bogus. This new wave of check scams just looks less bogus, more legitimate, and targets lawyers. It has hit close to home, too. The State Bar is aware of several Arizona lawyers who have been approached by the scammers, and a few who have taken the bait.

The checks that scammers send you, whether they are personal checks or cashier's checks, look and feel real, and may even fool bank tellers. The checks may even be from a legitimate business or corporation, but may have been written fraudulently.

In another variant of the scam, no checks are involved. Instead, money is transferred directly from another account into your trust account. The other account is often the account of someone who fell for another scam. Once again, when the scam is discovered your bank will cancel the deposit. You will lose your other client's money and you could be charged with the crime of money-laundering.

The following is a compilation of information from the Comptroller of the Currency (http://www.occ.treas.gov.ftp/bulletin/2007-2.html), National Fraud Information Center (http://www.fraud.org/tips/internet/fakecheck.htm), Internet Crime Complaint Center (http://www.ic3.gov/crimeschemes.aspx#item-3) and Federal Bureau of Investigation (http://www.fbi.gov/majcases/fraud/fraudschemes.htm) about the scams, with additional information we've added specifically for lawyers.

How these scams work

These scams work well for three reasons:

The scammer appears to send you "real" money - usually a cashier's check or certified check drawn on a U.S. bank (sometimes even a postal money order) - before asking you to wire or express-mail part or all of that money to the scammer or a third party. The scam relies on your belief that real cashier's and certified checks and postal money orders are more trustworthy than personal checks. However, the counterfeit checks or money orders that the scammers send are very well made and tough to identify as fake.

The scam is initiated in response to a legitimate activity, such as offering legal services and legal representation. In the original versions of the Nigerian scam, the "offer" arrives unsolicited, in a letter, an email or a fax.

Once the scammer is in touch with you, he often will chat via email or phone, talking about the legal services he needs. He appears friendly, sincere and aboveboard. He works hard to win your trust, but appearing trustworthy is the con artist's primary tool in getting you to act.

Specific red flags to keep in mind

You are asked to pay money out of your account. This is a five-star red flag. If you are asked to do this, run, don't walk, away from the "deal." The basic pattern of all the fake check scams is that the con artists will send you a "cashier's" or "certified" check (or postal money order) to deposit into your account. Then they will give you a reason to quickly wire or express part or all of the money out of your account to them or to some third party they identify. Often the wired money is to go to a foreign country.

You are asked to act very quickly. The scammers don't want you to have time to verify whether the cashier's check or certified check is authentic or counterfeit or to wait for the check to clear. The scammers typically ask you to wire cash as quickly as possible. They know that their fakes are very professional and usually will pass an initial visual inspection at the financial institution taking the deposit. Some counterfeits are so good that it may take weeks to identify the check as counterfeit. At that point, you are left holding the bag: the scam artists have your money and you may even be suspected of fraud.

Fake check scammers often claim to be in another country. That makes it difficult, they say, for them to do business in the U.S. so they need your help to receive payments by checks on U.S. banks. Often you are asked to wire the funds out of the country.
The deal is too good to be true. This old, smart consumer advice holds true in these cases. If a "client" is eager, sight unseen, to enlist your legal services, smell a rat. If after a few emails or phone conversations, a "client" wants to hire you, slow down.

Avoiding the scam

Wait for a cashier's or certified check to clear before using the money. Although your financial institution may quickly make funds available that you've deposited, or may tell you that the deposit has been credited to your account, that does not mean that the check is good or has cleared through the original issuing institution. That can take many days. Sometimes it can take weeks to discover a very good forgery, and the check won't bounce until then. Therefore, verify the check with the *issuing* bank and then wait for final clearance. All it will take is one insufficient-funds check for your trust account to be in the red. (And you know, of course, that banks have to report to the State Bar when your trust account becomes overdrawn?)

Don't be fooled into thinking that the company is real or legitimate just because its website looks good. Some of the sites run by scammers look extremely professional.

Know with whom you are dealing. The law generally assumes that you, not your financial institution, have the best knowledge of the person who gave you the check because you are dealing directly with them. Therefore, if you are dealing with a stranger, make sure you have that person's name address and phone number, then verify those independently using online directories. If the number or address in the directory is different, call the person using those numbers. You may have stumbled into an identity-theft situation and can help another consumer.

There is no legitimate reason for someone who is giving you money to ask you to wire money back. **Always insist that the check be in the exact amount or deal in cash. Emphasize that you prefer a check from a local bank or a national bank with a branch in your area.**

Your deposits are your responsibility. If you have deposited a check that then bounces, the bank will withdraw the original dollar amount credited to your trust account. If your trust account doesn't have enough money to cover the deduction, the bank may freeze your trust account or, worse, the bank may sue you to recover the funds. The problem for lawyers is that if you hold funds for clients or third parties, you have to hold it in your client trust account. As a result, in this scam, if you're complying with the ethical rules, you would have put the money into your trust account and then you're disbursing out of your trust account. If the check you deposit turns out to be fake, then you may have converted the other clients' funds in your account.

So what do you do if you've been ensnared in a scam?

If you've been scammed, call the State Bar's Ethics Hotline (602-340-7284) or the Trust Account Hotline (602-340-7305) and your bank for advice. If you find that you've taken a fake check, don't deposit it. If you want to report it, go to the website of the National Fraud Information Center, http://www.fraud.org/.

F. Credit Cards and IRS Section 6050W

If you accept debit or credit cards from clients, a new IRS rule could cause problems if you're not ready.

Starting January 1, 2013, attorneys who accept credit cards need to make sure that the names on their merchant accounts match the ones the IRS has on file. Some attorneys may have used abbreviations or acronyms when they opened their accounts. If there is not an EXACT match between the information provided to the credit card processing company and the information on file with the IRS, there may be serious consequences:

Beginning January 2013, the IRS will impose a 28% withholding penalty on all credit card transactions. That could include your IOLTA client trust account if the account isn't labeled properly.

Lawyers could also commit ethical violations if they are unable to gain access to client funds in IOLTA accounts by failing to take the proper precautions.

Most credit card companies notified merchant accounts about the change. Ultimately, however, it's your responsibility to make sure that the IRS has your correct information. Please take the following steps:

1. If you accept credit cards, contact your credit card processor to check the name on the account.
2. Make whatever changes are necessary to stay in compliance.

For more information on Section 6050W visit www.IRS.gov, call the State Bar's Ethics Hotline (602-340-7284) or the State Bar's Trust Account Hotline (602-340-7305).

SECTION XIII: THE MECHANICS OF A TRUST ACCOUNT INVESTIGATION

A. Why the Investigation Begins

Bar counsel have the power and duty to investigate all information coming to the attention of the State Bar, which, if true, would be grounds for discipline or transfer to disability inactive status. Bar counsel evaluate all information coming to their attention by "charge" or otherwise alleging lack of professionalism, misconduct or incapacity. "Charge" means any "allegation of misconduct or incapacity brought to the attention of the State Bar." Bar counsel may also request one or more trust account examiners or volunteer bar counsel to aid them in conducting investigations. Trust account examiners work under the supervision of staff bar counsel.

A trust account investigation is often initiated in one of many ways:

1. A complaint from a client.

2. A complaint from a disgruntled former spouse or former employee.

3. A complaint from a third party.

4. An overdraft notice from the lawyer's bank.

5. A complaint from another lawyer.

6. Referrals from judges.

7. The Internal Revenue Service and other government and police agencies.

Rule 43(f)(3) requires lawyers to maintain their trust accounts only with authorized financial institutions. The authorized financial institutions have filed an agreement with the State Bar of Arizona and the Arizona Foundation for Legal Services & Education to provide notification of all instruments that are presented against insufficient funds in trust accounts. Financial institutions are required to provide notification of whether the instrument is honored or dishonored.

The trust account examiner screens and investigates all NSF/overdraft reports submitted to the State Bar of Arizona from the financial institutions. The trust account examiner also investigates those times when bar counsel receive a screening file initiated by a complainant and there are underlying issues related to the client trust account.

B. What Happens During the Examination

The examiner reviews the notice of overdraft/returned item, then opens an investigative file. The examiner sends the lawyer an initial letter with a copy of the notice of overdraft/returned item for a response within 20 days. The letter requests a written response to include the circumstances surrounding the occurrence of overdraft and a request to attach all necessary documentation to support the explanation in the response. The lawyer has a duty to cooperate and respond promptly and truthfully. Respondent's first response must be sent to the complainant (if there is one) unless a protective order is issued for "good cause."

In the initial letter sent to the lawyer, any number of the following records that are needed to conduct an examination of a trust account may be requested:

1. Bank statements
2. Canceled checks
3. Duplicate deposit slips or equivalent
4. Individual client ledgers or equivalent
5. Administrative funds/bank charges ledger or the equivalent
6. General ledger/checkbook register
7. Accountings/explanations
8. Bank fees/administrative funds ledger
9. Monthly three-way reconciliation
10. Fee agreements, billing statements, time records

After the examiner receives all of the necessary information and documentation, it is reviewed and a daily balance spreadsheet is created. A daily balance spreadsheet is simply a reconstruction of the lawyer's trust account for the period of review. Copies of the bank statements, canceled checks, duplicate deposit slips, general ledger, bank fees ledger and individual client ledgers are used in combination to reconstruct the lawyer's client trust account.

The examiner reviews the complete explanation of events that resulted in the overdraft/returned item and determines whether the records provided by the lawyer support the explanation. The examiner looks to see whether the lawyer maintains the

required trust account records according to the Rules, has an understanding of the trust accounts as sub-accounts and for any unusual transactions.

The examiner then completes a detailed transaction analysis. Every transaction in and out of the trust account must correspond to a specific client's ledger, bank fees/administrative funds ledger, general ledger, and bank source document such as the account statement and canceled check or deposit slip.

After the transaction analysis is complete, the examiner issues a summary of findings that details those Rules regarding trust account maintenance that were violated. The final summary is submitted to bar counsel for review along with the file and all of its contents.

Some examples of significant trust account violations include:

1. Intentional misappropriation/conversion of client funds

2. Using trust account as operating account

3. No client ledgers

4. Inappropriate disbursements from trust account

5. Sizable amounts of personal monies in trust account (commingling).

Some common errors and oversights in the maintenance of trust accounts include:

1. Lawyer or law firm errors resulting in overdrafts and non-sufficient funds items:

    a. Deposit does not get delivered or credited to the trust account before the corresponding disbursements pay against the account. This may result in the conversion of other client funds in the trust account.
    b. Lawyer maintains two trust accounts, a deposit is credited to one trust account and corresponding disbursements are inadvertently drawn from the other trust account.
    c. Deposited item was returned for non-sufficient funds or improper endorsement after the corresponding disbursements have paid against the account.
    d. Errors in the calculation of settlement disbursements resulting in the client or lawyer being overpaid. This may result in the conversion of other client funds in the trust account.

2. Failure to properly maintain individual client ledgers or the equivalent.

3. Failure to maintain duplicate deposit slips or the equivalent.

4. Failure to reconcile individual client ledgers to the bank statements and the general ledger.

5. Improper transactions processed through the trust account.

6. Using the trust account as an operating account.

7. Using the trust account for family, associations and non-client related transactions.

8. Depositing earned fees into the trust account.

9. Cash-back deposits/client deposits not made intact.

10. ATM withdrawals, counter debits.

11. Maintaining a large balance of lawyer or law firm funds in the trust account.

12. Misunderstanding the bank's decision to grant immediate credit on deposited items as the funds actually being collected and therefore permissible to draw disbursements against the deposit.

SECTION XIV: FREQUENTLY ASKED QUESTIONS

Q. How do I know if I need to have a trust account?
A. If you are presently or potentially in the future going to be in possession of client or third party funds then you should set up a trust account. You also need to look at how you handle client costs. If the client advances payment of his/her costs then you would need to place those funds into your trust account. Even if the client pays you a flat fee with an advanced cost in one check, the check would need to be deposited into your trust account and then the flat fee portion would be transferred to your operating account once the check has cleared. Then you could pay the cost(s) from your trust account or reimburse yourself for costs you pay. An example of this type of transaction would be if you charge a flat $590 to do a corporation formation, $500 of the $590 is an earned upon receipt fee and the other $90 is for the filing fees. The entire $590 would be deposited into your trust account and then the $500 would be transferred to your operating account, once the check clears, and then you would issue a $90 trust account check to corporation commission for the filing of the corporation or a check to reimburse yourself for the filing fee in the event that you already paid it. *See* ER 1.15 and Rule 43. You can also contact the State Bar of Arizona's Trust Account Hotline at 602-340-7305 for additional information.

Q. How do I set-up a trust account?
A. Read ER 1.15 and Rule 43. You should also contact the State Bar of Arizona's Law Office Management Assistance Program for forms to take to your bank as well as other helpful trust account materials. You can also obtain forms from the Lawyer Resources page of the State Bar of Arizona's website at http://www.azbar.org/professionaldevelopment/lomap/forms.

Q. Which tax identification number is used for the trust account?
A. The tax identification number for any IOLTA account should be that of the Arizona Foundation for Legal Services & Education, 95-3351710, unless you fall under the exceptions to the rule. Your financial institution should be instructed to use the AZFLSE's tax identification number, not the tax identification number of the lawyer or law firm. As such, the lawyer or law firm should never receive IRS Form 1099 for trust account interest. This method of account identification allows the earned interest to be recorded annually in the name of the AZFLSE and not in the name of the lawyer/law firm. The name on the account, however, is to be that of the lawyer or law firm.

Q. What kinds of records do I need to maintain on my trust account?
A. Bank statements, canceled checks (unless microfilmed/imaged by your bank), other evidence of disbursement, duplicate deposit slips/equivalent, individual client ledgers/equivalent, trust account general ledger/checkbook register, reports to clients regarding their funds in the trust account, and three-way reconciliation reports. *See* Rule 43(b)(2).

Q. How long do I need maintain these records?
A. You need to keep trust account records for a period of five years after termination of the representation. *See* ER 1.15(a) and 43(b)(2)(A).

Q. What is an individual client ledger and what information needs to be captured on it?
A. A client ledger must include a record of all trust account transactions relating to a particular client, showing the date, amount and payor of each receipt of funds, the date, amount and payee of each disbursement of funds, and any unexpended balance. The ledger should include a description of the transaction and a running balance, i.e. total deposits minus disbursements. *See* Rule 43(b)(2)(B).

Q. May I wire transfer in and out of my trust account?
A. Yes, you can always wire funds into your trust account, and since December 3, 2003, you are permitted to wire transfer funds from your trust account provided a record is maintained. Telephone and online transfers are discouraged. Rule 43(b)(5).

Q. May a lawyer deposit her own funds into her client trust account in order to cover bank service charges?
A. Yes, but only in an amount necessary for that purpose. *See* ER 1.15(b) and Rule 43(a)(1).

Q. The bank gave me a debit/credit card for my trust account. May I use it?
A. No. Money can only be disbursed from the trust account by pre-numbered check or wire transfer with proper documentation. *See* Rule 43(b)(5).

Q. How do I handle credit card payments through my trust account?
A. You may deposit funds from a credit card transaction into a client trust account for payment of advance fees, costs or expenses, and merchant or credit card transaction fees, but only if you have a source of funds, other than client or third-party funds, available at the time of the credit card transaction to replace any funds that may be debited from the account due to a credit card chargeback and any associated fees or charges. *See* Rule 43(b)(3).

Q. What do I do with unclaimed money left in my trust account?
A. Try to make contact with the client or third party who is entitled to the funds and be sure to document your efforts. In the event that you are unsuccessful in locating the entity entitled to the funds, you should escheat the funds to unclaimed property department of the State of Arizona. *See* ER 1.15(d), (e), and ER 1.16(d) and Ariz. *Ethics Op.* 97-03.

Q. What are the components of a proper "three-way reconciliation" and how often do I have to do one?
A. The components of a three-way reconciliation are: Total of all client ledgers = Ending balance of the general ledger/checkbook register = Bank statement ending balance (plus/minus any outstanding deposits, checks, and interest). Determine the ledger totals and balances "as of the bank statement ending date." Also, if you have deposited

personal funds into the trust account to cover bank charges ("bank service charges" ledger), be sure to include this balance as well, when totaling your client ledgers. A three-way reconciliation of the trust account needs to occur on a monthly basis. *See* Rule 43(b)(2)(C).

Q. What if my client gives me a check today for work I will do tonight? I know I'm going to earn it right away. Do I deposit the check into my trust account or my operating account?

A. If you have not performed the work at the time the client gave you the money, then you must deposit it into the trust account prior to disbursing funds to pay yourself for the work you performed. *See* Rule 43(a).

Q. How long must I wait for a deposited check to clear before I can disburse against it?

A. You cannot disburse against uncollected funds. The State Bar advises attorneys to wait 10 business days before disbursing. Rule 43(b)(4) allows for earlier disbursement against "limited-risk deposits." *See* Rule 43(b)(4)(A) for description of "limited-risk deposits."

Q. I use a computer program to track my trust account activity. Do I need to keep manual "ledgers" too?

A. No. There are several computer programs that automate the process of keeping a trust account so that you do not need to keep manual records too. Just be certain that you have your computer program set up appropriately so that you can meet the requirements of proper trust record maintenance, including what to show on a transaction entry, how to easily view a client's funds, and how to perform a monthly reconciliation. Be sure you have a secure backup system in place. As an added security, you may keep monthly printouts of the trust account general ledger. *See* Rule 43(b)(2).

Q. I want to advance a cost for my client, should I advance it from my trust account?

A. No. You should only advance client costs (where you are paying on behalf of the client and then will be reimbursed by the client) from your operating account. *See* ER 1.15(c).

Q. May I have my legal assistant be a signer on the trust account?

A. The rules do not prohibit a non-lawyer as a signer on a client trust account. Consider, however, whether you want to have a non-lawyer as a signer, because you are ultimately responsible for any problems with the trust account. Planning in advance can avoid the need to have someone other than a lawyer be a signer on the trust account. *See* Rule 43(b)(1)(B).

Q. What types of funds should be deposited into my client trust account?

A. Funds belonging entirely to the client, funds belonging in part to a client and in part presently or potentially to the lawyer, funds belonging to a third party in connection with a representation, and personal funds in an amount necessary for that purpose to cover bank charges. *See* ER 1.15(b) and Rule 43(a).

Q. How do I handle client funds that are in dispute?

A. When in the course of representation, a lawyer in possession of property in which two or more persons (one of whom may be the lawyer) claim interests, the funds shall be kept separate with the client trust account until the dispute is resolved. The lawyer shall promptly distribute all portions of the property as to which the interests are not in dispute. *See* ER 1.15(e). You now have an option under ER 1.15(f) to notify the third party that you intend to distribute the funds to the client. You must give the third party written notice of your intent, serve it pursuant to Rule 4.1 or 4.2 of civil procedure rules, and allow the third party 90 days to notify you of any actions the third party plans to take. If you receive notice from the third party, then you must continue to hold the funds; if you do not receive notice from the third party, then you may distribute the funds to the client after getting the client's informed consent, in writing, to do so. This rule is not intended to alter a third parties substantive rights.

Q. Who gets the interest from my client trust account?

A. A lawyer or law firm receiving client funds shall maintain a pooled interest bearing or dividend-earning trust account for deposit of client funds where the interest or dividends reasonably expected to be earned thereon are nominal in amount. The interest or dividends accruing on this account, net of any service or other charges or fees imposed by the financial institution or investment company in connection with the account, shall be paid by the financial institution or investment company to the Arizona Foundation for Legal Services & Education, and shall be used solely for the following purposes: to pay the actual administrative costs of this interest or earnings on lawyers' trust accounts program; to fund programs designed to assist in the delivery of legal services to the poor; to support law-related education programs designed to teach young people, educators and other adults about the law, the legal process and the legal system; to fund studies or programs designed to improve the administration of justice; and to maintain a reasonable reserve therefore. *See* Rule 43(f)(6).

Q. What is a "limited-risk uncollectible deposit"?

A. Certain categories of trust account deposits are considered to carry a limited and acceptable risk of failure so that disbursements of trust account funds may be made in reliance on such deposits without disclosure to and permission of clients and third persons owning trust account funds that may be affected by such disbursements. Notwithstanding that a deposit made to the lawyer's trust account has not been finally settled and credited to the account, the lawyer may disburse funds from the trust account in reliance on such deposit under any of the following circumstances, if the lawyer has other sources of funds, other than client or third party funds, available at the time of disbursement to replace any uncollected funds:

i. when the deposit is made by certified check or cashier's check;
ii. when the deposit is made by a bank check, official check, treasurer's check, money order, or other such instrument where the payor is a bank, savings and loan association, or credit union;
iii. when the deposit is made by a check issued by the United States, State of Arizona, or any agency or political subdivision of the State of Arizona; or

iv. when the deposit is made by a check or draft issued by an insurance company, title insurance company, or a licensed title insurance agency authorized to do business in the state of Arizona.

See Rule 43(b)(4)(A).

Q. What types of disbursements are not allowed from my client trust account?

A. Disbursements by counter checks, cash-back transactions from deposits, and ATM card withdrawals. Online transfers and phone transfers are allowed if they provide an audit trail, but they are not considered safe. Otherwise disbursements must be made by pre-numbered check or electronic transfer. *See* Rule 43(b)(5).

Q. Once I have earned my fees on a client's case, can I write the trust account check for those earned fees to a third party, such as my landlord, instead of to myself?

A. Using a trust account as a lawyer's general checking account, even when the fees have been earned, may void the fiduciary status of the trust account and subject client funds to claims by other parties, including the lawyer's creditors. All disbursements on behalf of a lawyer should be made by pre-numbered check directly to the lawyer or law firm. Deposit the check into your operating account and then disburse as you wish.

Q. What happens if I don't have the correct trust account records?

A. Failure to maintain trust account records as required by ER 1.15 or Rule 43, establishes a rebuttable presumption that the lawyer has failed to properly safeguard client or third person's funds or property. *See* Rule 43(d)(3).

APPENDIX A: TRUST ACCOUNT RULES

ER 1.15. Safekeeping Property

(a) A lawyer shall hold property of clients or third persons that is in a lawyer's possession in connection with a representation separate from the lawyer's own property. Funds shall be kept in a separate account maintained in the state where the lawyer's office is situated, or elsewhere with the consent of the client or third person. Other property shall be identified as such and appropriately safeguarded. Complete records of such account funds and other property shall be kept by the lawyer and shall be preserved for a period of five years after termination of the representation.

(b) A lawyer may deposit the lawyer's own funds in a client trust account only for the following purposes and only in an amount reasonably estimated to be necessary to fulfill the stated purposes:

(1) to pay service or other charges or fees imposed by the financial institution that are related to operation of the trust account; or

(2) to pay any merchant fees or credit card transaction fees or to offset debits for credit card chargebacks.

(3) Earned fees and funds for reimbursement of costs or expenses may be deposited into a trust account if they are part of a single credit card transaction that also includes the payment of advance fees, costs or expenses and the lawyer does not use a credit card processing service that permits the lawyer to direct such funds to the lawyer's separate business account. Any such earned fees and funds for reimbursement of costs or expenses must be withdrawn from the trust account within a reasonable time after deposit.

(c) A lawyer shall deposit into a client trust account legal fees and expenses that have been paid in advance, to be withdrawn by the lawyer only as fees are earned or expenses incurred.

(d) 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 between the client and the 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.

(e) When in the course of representation a lawyer possesses property in which two or more persons (one of whom may be the lawyer) claim interests, the property shall be kept separate by the lawyer. The lawyer shall promptly distribute any portions of the property

as to which there are no competing claims. Any other property shall be kept separate until one of the following occurs:

(1) the parties reach an agreement on the distribution of the property;

(2) a court order resolves the competing claims; or

(3) distribution is allowed under section (f) below.

(f) Where the competing claims are between a client and a third party, the lawyer may provide written notice to the third party of the lawyer's intent to distribute the property to the client, as follows:

(1) The notice shall be served on the third party in the manner provided under Rules 4.1 or 4.2 of the Arizona Rules of Civil Procedure, and must inform the third party that the lawyer may distribute the property to the client unless the third party initiates legal action and provides the lawyer with written notice of such action within 90 calendar days of the date of service of the lawyer's notice.

(2) If the lawyer does not receive such written notice from the third party within the 90-day period, and provided that the disbursement is not prohibited by law or court order, the lawyer may distribute the funds to the client after consulting with the client regarding the advantages and disadvantages of disbursement of the disputed funds and obtaining the client's informed consent tothe distribution, confirmed in writing.

(3) If the lawyer is notified in writing of an action filed within the 90-day period, the lawyer shall continue to hold the property separate unless and until the parties reach an agreement on distribution of the property, or a court resolves the matter.

(4) Nothing in this rule is intended to alter a third party's substantive rights.

COMMENT [2003 AMENDMENT]

[1] A lawyer should hold property of others with the care required of a professional fiduciary. Securities should be kept in a safe deposit box, except when some other form of safekeeping is warranted by special circumstances. All property which is the property of clients or third persons, including prospective clients, must be kept separate from the lawyer's business and personal property and, if monies, in one or more trust accounts. Separate trust accounts may be warranted when administering estate monies or acting in similar fiduciary capacities. A lawyer should maintain on a current basis books and records in accordance with generally accepted accounting practice and comply with any recordkeeping rules established by law or court order. *See* Supreme Court Rules 43(i) and 44.

[2] While normally it is impermissible to commingle the lawyer's own funds with client funds, paragraph (b) provides that it is permissible when necessary to pay bank service charges on that account. Accurate records must be kept regarding which part of the funds are the lawyer's.

[3] Lawyers often receive funds from which the lawyer's fee will be paid. The lawyer is not required to remit to the client funds that the lawyer reasonably believes represent fees owed. However, a lawyer may not hold funds to coerce a client into accepting the lawyer's contention. The disputed portion of the funds must be kept in a trust account and the lawyer should suggest means for prompt resolution of the dispute, such as arbitration. The undisputed portion of the funds shall be promptly distributed.

[4] [Effective December 1, 2004] The Rule also recognizes that third parties may have just claims against specific funds or other property in a lawyer's custody, such as a client's creditor who has a lien on funds recovered in a personal injury action. A lawyer may have a duty under applicable law to protect such third-party claims against wrongful interference by the client. In such cases, when the third-party claim has become a matured legal or equitable claim, and unless distribution is otherwise allowed under this rule, the lawyer must refuse to surrender the property to the client until the claims are resolved. In addition to the procedures described in this rule, when there are substantial grounds for dispute as to the person entitled to the funds, the lawyer may file an action to have a court resolve the dispute.

[5] The obligations of a lawyer under this Rule are independent of those arising from activity other than rendering legal services. For example, a lawyer who serves only as an escrow agent is governed by the applicable law relating to fiduciaries even though the lawyer does not render legal services in the transaction and is not governed by this Rule.

[6] A lawyer's fund for client protection provides a means through the collective efforts of the bar to reimburse persons who have lost money or property as a result of dishonest conduct of a lawyer. Where such a fund has been established, a lawyer must participate where it is mandatory, and, even when it is voluntary, the lawyer should participate. Every lawyer has a professional obligation to participate in the collective efforts of the bar to reimburse clients and escrow beneficiaries who have lost money or property as the result of dishonest conduct in the practice of law. A lawyer's financial contribution to a lawyers' fund for client protection is an acceptable method of fulfilling this obligation.

[7] For further obligations regarding client property and trust accounts, see Supreme Court Rule 43 ("Trust Account Verification") and Rule 44 ("Trust Accounts, Interest Thereon").

COMMENT [2009 AMENDMENT]

[1] The 2009 amendments to E.R. 1.15 correspond with the 2009 amendments to Supreme Court Rule 43 on Trust Accounts. Supreme Court Rule 43 and the 2009

comments thereto contain additional requirements and procedures governing credit card transactions.

[2] For purposes of this rule, "merchant fees" and "credit card transaction fees" are fees that are deducted from the amount of the credit card charge to pay the company that issued the client's credit card, the lawyer or law firm's credit card processing service, and the credit card association (e.g., Visa, MasterCard), and related charges. Those fees typically include a percentage of the total amount billed plus a fixed fee, which, unless paid by the lawyer or law firm, reduces the amount that can be credited to the client's account. A "chargeback" (or reversal of charges) occurs when a client or former client writes to the credit card company that issued the credit card used to pay a lawyer to dispute the amount that should be paid to the lawyer or law firm. When a client or former client does so, the lawyer's or law firm's account is debited an amount equal to the disputed amount, plus a chargeback fee.

[3] Lawyers and law firms are permitted, and in some cases may be required, to place their own funds into their trust accounts in very limited circumstances. Lawyers and law firms that accept payment by credit card for advance fees, costs or expenses must at all times maintain in their trust accounts sufficient funds of their own to pay fees and charges related to operation of the trust account, and to pay all merchant and credit card transaction fees, chargeback fees and related charges. Lawyers and law firms must make a reasonable determination of the amount of their own funds that may appropriately be kept in their trust accounts to pay trust account and credit card fees and charges. Lawyers and law firms that use credit card processing services that debit all chargebacks and credit card fees and charges from an operating or business account are not required to maintain their own funds in their trust accounts to cover those charges, since no client or third-party funds will be at risk due to debits from the trust account. Lawyers should consult Rule 43 on the circumstances when lawyer funds are required to be maintained in a trust account to avoid misappropriation or conversion of client or third-party funds.

COMMENT [2014 AMENDMENT]

[1] New paragraph (f) allows a lawyer to distribute funds or property in the lawyer's possession after providing notice to third persons known to claim an interest. Notice under paragraph (f) must be sufficient to allow the third person to take appropriate action to protect its interests. Although there is no one form of notice that will be acceptable, the notice should generally include at least the following: (a) a description of the funds or property in the lawyer's possession; (b) the name of the client claiming an interest in the funds and other information reasonably available to the lawyer that would allow the third person to identify the claim or interest; (c) a mailing address, telephone number, and email address where the third party can provide notice to the lawyer of the commencement of an action asserting an interest in the funds or property; and (d) the proposed distribution of the funds or property. The notice shall be served in the manner provided under Rules 4.1 or 4.2 of the Arizona Rules of Civil Procedure.

[2] Apart from their ethical obligations, lawyers may have legal obligations to safeguard third-party funds under applicable case and statutory law. The notice provisions of paragraph (f) do not alter a lawyer's legal obligations and duties to third persons with respect to funds or property in the lawyer's possession. A lawyer who proposes to distribute funds under this paragraph should carefully evaluate the underlying law governing the lawyer's obligations to safeguard funds in which third persons claim an interest, which may expose the lawyer to a risk of civil or other liability even if the notice provisions of paragraph (f) are satisfied.

[3] Before making any distribution of funds or property pursuant to paragraph (f), a lawyer should explain to the client that the client may remain responsible to satisfy valid claims of third persons, and that the third person's failure to commence an action within the 90-day period of paragraph (f) will not by itself operate to waive, reduce or extinguish the third person's claim, if any, against the client or the funds or property received by the client. Before making any distribution under paragraph (f), the lawyer must obtain the client's informed consent, confirmed in writing, to the distribution.

Rule 43. Trust Accounts

(a) Duty to Deposit Client Funds and Funds Belonging to Third Persons; Deposit of Funds Belonging to the Lawyer. Funds belonging in whole or in part to a client or third person in connection with a representation shall be kept separate and apart from the lawyer's personal and business accounts. All such funds shall be deposited into one or more trust accounts that are labeled as such. The location of the trust account shall be controlled by the provisions of ER 1.15(a). No trust account required by this rule may have overdraft protection. No funds belonging to the lawyer or law firm shall be deposited into a trust account established pursuant to this rule except as follows:

1. Funds to pay service or other charges or fees imposed by the financial institution that are related to operation of the trust account, but only in an amount reasonably estimated to be necessary for that purpose may be deposited therein.

2. Funds to pay merchant fees or credit card transaction charges or to offset debits for credit card chargebacks, but only in an amount reasonably estimated to be necessary for those purposes may be deposited therein.

3. Earned fees and funds for reimbursement of costs or expenses may be deposited into a trust account if they are part of a single credit card transaction that also includes the payment of advance fees, costs or expenses and the lawyer does not use a credit card processing service that permits the lawyer to direct such funds to the lawyer's separate business account. Any such earned fees and funds for reimbursement of costs or expenses must be withdrawn from the trust account within a reasonable time after deposit.

4. Funds belonging in part to a client or third person and in part presently or potentially to the lawyer or law firm must be deposited therein, but the portion belonging to the lawyer or law firm must be withdrawn when due and legally available from the financial institution, or within a reasonable time thereafter, unless the right of the lawyer or law firm to receive it is disputed by the client or third person, in which event the lawyer shall comply with ER 1.15(e).

(b) Trust Account Requirements.

1. Standards of Performance.

A. Due professional care must be exercised in the performance of the lawyer's duties under this rule.

B. Employees and others assisting the attorneys in the performance of such duties must be competent and properly trained and supervised.

C. Internal controls within the lawyer's office must be adequate under the circumstances to safeguard funds or other property held in trust.

2. Trust Account Records.

A. Every active member of the state bar shall maintain, on a current basis, complete records of the handling, maintenance and disposition of all funds, securities and other property belonging in whole or in part to a client or third person in connection with a representation. These records shall include the records required by ER 1.15 and cover the entire time from receipt to the time of final disposition by the lawyer of all such funds, securities and other property. The lawyer shall preserve these records for a period of five years after termination of the representation.

B. A lawyer shall maintain or cause to be maintained an account ledger or the equivalent for each client, person or entity for which funds have been received in trust, showing:

(i) the date, amount and payor of each receipt of funds;

(ii) the date, amount and payee of each disbursement; and

(iii) any unexpended balance.

C. A lawyer shall make or cause to be made a monthly three-way reconciliation of the client ledgers, trust
account general ledger/checkbook register, and the trust account bank statement.

D. A lawyer shall retain, in accordance with this rule, all trust account bank statements, cancelled prenumbered checks (unless recorded on microfilm or stored electronically by a bank or other financial institution that maintains such records for the length of time required by this rule), other evidence of disbursements, duplicate deposit slips or the equivalent (which shall be sufficiently detailed to identify each item), client ledgers, trust account general ledger/checkbook register, and reports to clients.

E. A record shall be maintained showing all property, other than cash, held for clients or third persons in connection with a representation, including the date received, where located and when returned or otherwise distributed.

3. Deposits from Credit Card Transactions. A lawyer or law firm may permit funds from a credit card transaction to be deposited into a client trust account for payment of advance fees, costs or expenses, and merchant or credit card transaction fees, but only if:

A. the lawyer has sources of funds, other than client or third-party funds, available at the time of the credit card transaction to replace any funds that may be debited from the account due to a credit card chargeback and any associated fees or charges;

B. within three business days of receipt of notice or actual knowledge that a chargeback has been made, the lawyer deposits into the trust account his or her own funds in an amount equal to the amount of the chargeback that exceeds the client's credit card funds remaining in the trust account, and any fees or charges associated with the chargeback; and

C. the trust account contains sufficient funds of the lawyer or law firm at the time of the transaction to pay all merchant and credit card transaction fees, except to the extent such fees are paid by the client as part of the transaction.

4. Disbursement Against Uncollected Funds. A lawyer generally may not use, endanger, or encumber money held in trust for a client or third person without the permission of the owner given after full disclosure of the circumstances. Except for disbursements based upon any of the four categories of limited-risk uncollected deposits enumerated in paragraph A below, a lawyer may not disburse funds held in trust unless the funds are collected funds. For purposes of this provision, “collected funds” means funds deposited, finally settled by the issuer's bank, and credited without recourse to the lawyer's trust account.

A. Certain categories of trust account deposits are considered to carry a limited and acceptable risk of failure so that disbursements of trust account funds may be made in reliance on such deposits without disclosure to and permission of clients and third persons owning trust account funds that may be affected by such disbursements. Notwithstanding that a deposit made to the lawyer's trust account has not been finally settled and credited to the account, the lawyer may disburse funds from the trust account in reliance on such deposit under any of the following circumstances, if the lawyer has other sources of funds, other than client or third party funds, available at the time of disbursement to replace any uncollected funds:

(i) when the deposit is made by certified check or cashier's check;

(ii) when the deposit is made by a bank check, official check, treasurer's check, money order, or other such instrument where the payor is a bank, savings and loan association, or credit union;

(iii) when the deposit is made by a check issued by the United States, the State of Arizona, or any agency or political subdivision of the State of Arizona; or
(iv) when the deposit is made by a check or draft issued by an insurance company, title insurance company, or a licensed title insurance agency authorized to do business in the state of Arizona.

In any of the above circumstances, a lawyer's disbursement of funds from a trust account in reliance on deposits that are not yet collected funds is at the risk of the lawyer making the disbursement. If any of the deposits fail, for any reason, the lawyer, upon receipt of notice or actual knowledge of the failure, must immediately act to protect the property of the lawyer's clients and third persons. If the lawyer accepting any such check personally pays the amount of any failed deposit within three business days of receipt of notice that the deposit has failed, the lawyer will not be considered to have committed professional misconduct based upon the disbursement of uncollected funds.

B. A lawyer's disbursement of funds from a trust account in reliance on deposits that are not yet collected funds in any circumstances other than those four categories set forth above, when it results in funds of clients or third persons being used, endangered, or encumbered, will be grounds for a finding of professional misconduct.

5. Methods of Disbursement. All trust account disbursements shall be made by pre-numbered check or by electronic transfer, provided the lawyer maintains a record of such disbursements in accordance with the requirements of this rule. All instruments of disbursement shall be identified as a disbursement from a trust account.

(c) Certificate of Compliance. Every active member of the state bar shall on or before February 1 of each year file with the board a certificate certifying compliance with the provisions of this rule and ER 1.15 of the Arizona Rules of Professional Conduct, or that he or she is exempt from the provisions of this rule and ER 1.15. The certificate of compliance shall state as follows:

Annual Certificate of Compliance
I have read Rule 43, Rules of the Supreme Court, and ER 1.15, Arizona Rules of Professional Conduct, and certify that I am in compliance with the provisions thereof, or am exempt from such provisions as therein provided.

Dated: _____
Signature: _____
Type or print name: _____

As an alternative to filing a written certificate, the board may allow certification to be filed electronically in a method and form as approved by the board.

(d) Trust Account Examination; Random Examination.

1. Authority. The state bar shall evaluate all information coming to its attention by charge or otherwise indicating a possible violation of the trust account rules, and such information shall be treated and processed as is any other charge against a lawyer. In addition to trust account examinations that shall be conducted based upon information

coming to the bar's attention, the state bar may also conduct random trust account examinations of any member's trust account(s), in accordance with Guidelines developed by the Board of Governors and approved by the supreme court.

2. Scope of Examination. The state bar may verify all funds, securities and other property held in trust by the member, and all related accounts, safe deposit boxes, and any other form of maintaining trust funds, securities or property, together with deposit slips, cancelled checks, and all other records pertaining to transactions concerning trust funds, securities and property.

3. Rebuttable Presumption. If a lawyer fails to maintain trust account records required by this rule or ER 1.15, or fails to provide trust account records to the state bar upon request or as ordered by a panelist, a hearing officer, the commission or the court, there is a rebuttable presumption that the lawyer failed to properly safeguard client or third person's funds or property, as required by this rule and ER 1.15.

4. Limited Exception for Out-of-State Members. All funds, securities and other property of clients and third persons held by an Arizona-licensed lawyer whose law office is situated in another state shall not be subject to investigation, examination or verification except to the extent such funds and property are related to matters affecting Arizona clients.

5. Trust Account Examination and Verification Expenses. A member whose trust account has been examined or verified pursuant to this rule shall not be responsible for the costs and expenses related to the examination or verification, unless such costs and expenses are imposed pursuant to an order of diversion as set forth in Rule 55(a) or in conjunction with imposition of a disciplinary sanction as set forth in Rule 54(b) or Rule 60(b).

(e) Confidentiality. The provisions of Rule 70(b) of these rules shall apply to records acquired during examinations conducted pursuant to this rule. In those instances where the state bar conducts a random examination of a member's trust account(s) that does not result in a disciplinary charge, all information received as a result of that examination shall be kept strictly confidential and shall not be released to any person(s).

(f) Establishment of Trust Accounts; State Bar Oversight.

1. A lawyer or law firm receiving funds belonging in whole or in part to a client or third person in connection with a representation must hold the funds in one of the following types of accounts:

A. a pooled interest-bearing or dividend-earning trust account ("IOLTA account") on which the interest or dividends accrue for the benefit of the Arizona Foundation for Legal Services and Education ("Foundation");

B. a separate interest-bearing or dividend-earning trust account for the particular client or client's matter on which the interest or dividends, net of any reasonable service or other charges or fees imposed by the financial institution or investment company in connection with the account, will be paid to the client; or

C. a pooled interest-bearing or dividend-earning trust account, with subaccounting provided by the lawyer or the law firm, which will provide for computation of interest or dividends earned by each client's funds and the payment thereof, net of any reasonable service or other charges or fees imposed by the financial institution or investment company in connection with the account, to the client.

2. In determining which type of account provided for in section (f)(1) to use, a lawyer or law firm shall take into consideration the following factors:

A. the amount of funds to be deposited;

B. the expected duration of the deposit, including the likelihood of delay in the matter for which the funds are held;

C. the rates of interest or yield at financial institutions where the funds are to be deposited;

D. the cost of establishing and administering a separate non-IOLTA account for the client's benefit, including service charges, the costs of the lawyer's services, and the costs of preparing any tax reports required for income accruing to the client's benefit;

E. the capability of financial institutions to calculate and pay income to individual clients; and

F. any other circumstances that affect the ability of the client's funds to earn a net return for the client.

Funds should be deposited in an IOLTA account as provided for in section (f)(1)(A) if the interest does not cover the cost of opening and maintaining a separate interest-bearing or dividend-earning account. The State Bar shall not pursue a disciplinary matter against any lawyer or law firm solely based on the good-faith determination of the appropriate account in which to deposit or invest client funds.

3. A lawyer or law firm must maintain any client trust account provided for in section (f)(1) only at a regulated financial institution, which is either (i) a financial institution authorized by federal or state law to take deposits and conduct financial transactions with Arizona lawyers and is insured by the Federal Deposit Insurance Corporation or any successor insurance corporation(s) established by federal or state laws or (ii) any open-ended investment company registered with the Securities and Exchange Commission that is

authorized by federal or state law to take deposits and conduct financial transactions with Arizona lawyers. A regulated financial institution must agree to comply with the requirements of section (f)(4) below and agree to pay IOLTA interest to the Foundation. The lawyer or law firm must ensure that:

A. withdrawals or transfers can be made on demand, subject only to any notice period which the institution is required to reserve by law or regulation, and

B. the deposited funds are invested in the higher earning return of:

i. an interest-bearing checking account;

ii. a money-market deposit account with or tied to checking;

iii. a sweep account, which is a money-market fund or daily (overnight) financial institution repurchase agreement invested solely in or fully collateralized by U.S. Government Securities; or

iv. an open-end money-market fund solely invested in or fully collateralized by U.S. Government Securities.

A daily financial institution repurchase agreement may be established only with a regulated institution that is "well capitalized" or "adequately capitalized" as those terms are defined by applicable federal statutes and regulations. An open-end money market fund must be invested solely in U.S. Government Securities or repurchase agreements fully collateralized by U.S. Government Securities, must hold itself out as a "money-market fund" as that term is defined by federal statutes and regulations under the Investment Company Act of 1940, and at the time of the investment must have total assets of at least $250,000,000. "U.S. Government Securities" refers to U.S. Treasury obligations and obligations issued or guaranteed as to principal and interest by the United States or any agency or instrumentality thereof.

C. All service charges to the account are reasonable, related to the cost of maintaining the account, and computed in accordance with the financial institution's standard accounting practices.

D. The financial institution sends notification immediately to the State Bar chief bar counsel of any properly payable instrument that is presented for payment against a client trust account containing insufficient funds, uncollectible funds, or a negative available balance, regardless of whether the financial institution honors the instrument. All occurrences shall be reported to the State Bar regardless of the cause.

If a financial institution ceases to operate as a regulated financial institution and has no successor operating as a regulated financial institution, a lawyer or law firm that maintains

an account listed under section (f)(1) at that financial institution must, upon receiving notice of the financial institution's change in status, promptly notify any clients whose funds may be affected by the change in status, promptly transfer, to the extent possible, any client trust account funds from that financial institution into another account provided for in section (f)(1), and promptly deposit into the other account provided for in section (f)(1) any insurance, collateral, or proceeds resulting from the financial institution's change in status.

4. In addition to the requirements of section (f)(3), a lawyer or law firm may only maintain an IOLTA account as provided for in section (f)(1)(A) at an authorized regulated financial institution. To be designated as authorized, a regulated financial institution must sign a participation certification before the fiscal year beginning July 1, with the State Bar as representative of its members, and the Foundation as a third-party beneficiary and administrator of the interest or dividends.

A. The participation certification must:

i. define a reasonable charge for managing IOLTA accounts, which may include fees for reporting and recordkeeping;

ii. direct that interest or dividends, net of any reasonable service charges or fees, be remitted at least quarterly to the Foundation;

iii. provide that the financial institution transmit, with each remittance to the Foundation, a statement, as directed by the Foundation, showing information including the name of the lawyer or law firm on whose account the remittance is sent, the period for the remittance submitted, the account number, the account status, the rate of interest applied or the dividends earned, and the charges imposed against the interest remitted;

iv. provide that the financial institution transmit a report on each separate account, similar to the report required by section (f)(4)(a)(iii), to the lawyer or law firm opening said trust account;

v. direct that if the financial institution receives a subpoena duces tecum requesting documents pertaining to a lawyer's IOLTA account with the financial institution, the financial institution shall provide the documents specified in the subpoena duces tecum;

vi. provide that the terms apply to all branches of the regulated financial institution holding Arizona IOLTA accounts;

vii. provide that the financial institution be allowed to charge a particular lawyer or law firm for the reasonable cost of producing the reports and records required by this rule;

viii. provide that the participation certification may not be cancelled by the regulated financial institution except upon 30 days' advance written notice to the State Bar and the Foundation;

ix. provide that the participation certification may not be cancelled or revoked except upon 30 days' advance written notice to the regulated financial institution;

x. provide for an annual approval period; and

xi. provide that any participation certification continues in existence during any time the authorized regulated financial institution is attempting to become reauthorized.

B. If an authorized regulated financial institution does not sign the participation certification for the fiscal year beginning July 1 during which the regulated financial institution wishes to be re-authorized:

i. The matter will be referred to a mediator selected by the Court.

ii. The mediator will have 60 days to meet with the parties and attempt to reach a settlement.

iii. If after 60 days with mediation the parties do not reach a participation certification as provided for in section (f)(4)(A) above, the State Bar shall:

(a) notify the Supreme Court that the financial institution has failed to sign a participation certification for the following fiscal year;

(b) notify members who maintain trust accounts at that regulated financial institution that the regulated financial institution has failed to sign a participation certification for the following fiscal year; and

(c) notify other members that the regulated financial institution is not in compliance and that no new trust accounts may be opened at that financial institution for the following fiscal year.

iv. Upon receiving the State Bar's request provided for in section (f)(4)(B)(iii)(a), the Court may issue an order de-authorizing a previously authorized regulated financial institution that is seeking to become reauthorized.

C. The State Bar and the Foundation shall ensure the maintenance of a website listing of authorized regulated financial institutions' status.

5. If the State Bar and the Foundation become aware of information indicating that an authorized regulated financial institution has not complied with the duties provided for in section (f), the State Bar shall notify the regulated financial institution of its failure to comply and that it has 90 days to cure its noncompliance.

A. If, after 45 days, the noncompliance has not been cured, then the State Bar shall:

i. notify members who maintain trust accounts at that regulated financial institution that the regulated financial institution had been given 90 days to cure its noncompliance and to date it has not complied;

ii. notify other members that the regulated financial institution is not in compliance and that no new trust accounts may be opened at that financial institution;

iii. notify the Supreme Court that the financial institution is in noncompliance and had been given 90 days to cure its noncompliance.

B. If the financial institution cures its noncompliance, the State Bar shall promptly notify its members and the Supreme Court.

C. If the financial institution fails to cure the noncompliance, the State Bar shall file with the Court a request for termination of authorized status of that financial institution.

D. The Court may issue an order terminating the authorized status of the financial institution and instructing the State Bar to:

i. assure removal of the institution from the list of authorized financial institutions, and

ii. notify all members of the removal.

E. Upon receiving the notice provided for in section (f)(5)(D):

i. Members who maintain trust accounts at the de-authorized financial institution shall:

(a) have 90 days to transfer their accounts to an authorized financial institution, and

(b) by the end of 90 days, notify the State Bar that their trust accounts have been transferred and provide pertinent account information.

ii. Members who continue to maintain trust accounts at the de-authorized financial institution more than 90 days after notice or who fail to tell the State Bar that they have done so shall be referred to the State Bar Lawyer Regulation Office.

6. Interest or dividends generated on accounts specified in section (f)(1)(A) shall be paid by the financial institution or investment company to the Foundation. The Foundation shall use the interest or dividends solely to:

A. support programs designed to assist in the delivery of legal services to the poor and law-related education programs designed to teach young people, educators and other adults about the law, the legal process and the legal system;

B. fund studies or programs designed to improve the administration of justice;

C. maintain a reasonable reserve; and

D. pay the actual costs of administering this rule and the activities set forth above.

7. In addition to other obligations under section (f) of this rule, all lawyers admitted to practice in this state shall:

A. as a condition thereof, consent to the reporting and production requirements set forth in this rule, and

B. provide information requested by the State Bar on the annual dues statement regarding any and all client trust accounts they maintain.

(g) Reserved.

(h) Suspension of Member. Any active member who fails to comply with requirements of this rule shall be suspended summarily by order of the board upon notice by the state bar pursuant to Rule 62(a)(4), provided that a notice by certified, return receipt mail of such non-compliance shall have been sent to the member, mailed to the member's last address of record in the state bar office at least thirty days prior to such suspension.

(i) Reinstatement of Member. A lawyer who has been suspended for failure to comply with this rule may be reinstated by compliance with those provisions and notice to the board by the state bar of such compliance.

(j) Applicability of Rule. Every lawyer admitted to practice law in Arizona shall comply with the provisions of this rule regarding funds received, disbursed or held in Arizona, and funds received, disbursed or held on behalf of an Arizona client or a third person in connection with the representation of an Arizona client.

Amended April 26, 1994, effective June 1, 1994; April 27, 1998, effective July 1, 1998. Amended and effective Oct. 6, 2000.

Amended June 9, 2003, effective Dec. 1, 2003; Sept. 16, 2008, effective Jan. 1, 2009. Amended on emergency basis effective Jan. 1, 2009. Adopted on a permanent basis and amended effective Sept. 3, 2009. Amended Sept. 2, 2010, effective Jan. 1, 2011.

NOTES TO 2008 AMENDMENTS

This rule replaces former Rule 43 and 44 and authorizes the state bar to conduct random examinations of a member's trust account, in accordance with guidelines approved by the supreme court.

COMMENT [2009 AMENDMENT]

[1] In an attempt to balance the need to safeguard client and third-party property and encourage access to legal services to those who need them, lawyers may allow funds from credit card transactions to be deposited into their client trust accounts for advance fees, costs or expenses, and merchant or credit card transaction fees related thereto. Lawyers who choose to accept credit card payments for advance fees, costs or expenses must comply with the procedures and requirements in this rule. Permitting the deposit of funds from a credit card transaction into a client trust account for payment of advance fees, costs or expenses, and merchant or credit card transaction fees is at the risk of the lawyer permitting the deposit.

[2] For purposes of this rule, “merchant fees” and “credit card transaction fees” are fees that are deducted from the amount of the credit card charge to pay the company that issued the client's credit card, the lawyer or law firm's credit card processing service, the credit card association (e.g., Visa, Master-Card) and related charges. Those fees typically include a percentage of the total amount billed plus a fixed fee, which, unless paid by the lawyer or law firm, reduces the amount that can be credited to the client's account. A “chargeback” (or reversal of charges) occurs when a client or former client writes to the credit card company that issued the credit card used to pay a lawyer to dispute the amount that should be paid to the lawyer or law firm. When a client or former client does so, the lawyer's or law firm's account is debited an amount equal to the disputed amount, plus a chargeback fee.

[3] The rule prohibits funds belonging to the lawyer or law firm from being deposited into a trust account except in limited circumstances. The rule allows earned fees and funds for reimbursement of costs or expenses to be deposited temporarily into the trust account only when those funds are part of a single credit card transaction that includes payment of advance fees, costs and expenses, and the lawyer does not use a credit card processing service that permits the lawyer or law firm to identify the account into which funds from each credit card transaction should be deposited. Nothing in this rule prohibits lawyers from using one credit card account for the payment of earned fees and

reimbursement of costs or expenses (with deposits made into an operating or business account) and another credit card account for the payment of advance fees, costs or expenses (with deposits made into the trust account).

[4] To further protect client and third-party funds, lawyers and law firms should strive to use a credit card processing service that, at the lawyer's direction, will deposit advance fees, costs and expenses into the trust account and will debit the operating or business account for all fees and charges related to credit card transactions.

[5] Lawyers and law firms that accept payment by credit card for advance fees, costs or expenses must at all times maintain sufficient funds of their own in their trust accounts to ensure that no bank or credit card fees or charges results in the conversion or misappropriation of funds belonging to clients or third parties.

A lawyer violates this rule by failing to make the required deposit within three business days of receipt of notice or actual knowledge that a chargeback has been made to the trust account.

[6] When credit card funds are appropriately deposited into a trust account, any merchant or credit card transaction fees paid by the client as part of the credit card transaction must remain in the trust account until those funds are debited from the account. A lawyer or law firm, however, may agree to pay merchant or credit card transaction fees for the client. In that event, the lawyer or law firm must have funds of their own in their trust account in an amount at least equal to the merchant or credit card transaction fees before conducting the transaction. A failure to do so will result in the conversion or misappropriation of client or third-party funds when the merchant or credit card transaction fees are debited from the trust account. Lawyers and law firms must make a reasonable determination of the amount of their own funds that may appropriately be kept in their trust accounts to pay such fees and charges. Lawyers who maintain an unreasonable amount of their own funds in their trust accounts may be subject to a finding of misconduct.

[7] Lawyers and law firms that use credit card processing services that debit all chargebacks and credit card fees and charges from an operating or business account are not required to maintain their own funds in their trust accounts to pay such fees and charges, as no client or third-party funds will be at risk due to debits from the trust account.

APPENDIX B: EXAMPLE FORMS

A. Deposit Slip for One Client

PLEASE ENDORSE ALL CHECKS		
DATE 05/01/2017		
CHECKS AND OTHER ITEMS ARE RECEIVED FOR DEPOSIT SUBJECT TO THE RULES AND REGULATIONS OF THIS INSTITUTION. DEPOSITS MAY NOT BE AVAILABLE FOR IMMEDIATE WITHDRAWAL. PLEASE LIST EACH CHECK SEPARATELY.		
	DOLLARS	**CENTS**
CURRENCY		
COIN		
1 Alpha	$5,000	00
2		
3		
4		
5		
6		
7		
8		
9		
10		
11		
12		
13		
14		
15		
FRONT SIDE TOTAL	$5,000	00
REVERSE SIDE TOTAL	0	00
TOTAL DEPOSIT	$5,000	00

! ! ! ! ! ! ! ! !

Deposit slips should always be printed with the name of the lawyer or law firm, IOLTA or Trust Account Designation, account number, and routing number.

! ! ! ! ! ! ! ! !

B. Deposit Slip for Multiple Clients

PLEASE ENDORSE ALL CHECKS		
DATE 05/15/2017		
CHECKS AND OTHER ITEMS ARE RECEIVED FOR DEPOSIT SUBJECT TO THE RULES AND REGULATIONS OF THIS INSTITUTION. DEPOSITS MAY NOT BE AVAILABLE FOR IMMEDIATE WITHDRAWAL. PLEASE LIST EACH CHECK SEPARATELY.		
	DOLLARS	**CENTS**
CURRENCY		
COIN		
1 Beta	$1,500	00
2 Gamma	$1,450	00
3 Delta	$5,100	00
4 Epsilon	$3,400	00
5		
6		
7		
8		
9		
10		
11		
12		
13		
14		
15		
FRONT SIDE TOTAL	$10,050	00
REVERSE SIDE TOTAL	0	00
TOTAL DEPOSIT	$10,050	00

! ! ! ! ! ! ! ! !

Deposit slips should always be printed with the name of the lawyer or law firm, IOLTA or Trust Account Designation, account number, and routing number.

! ! ! ! ! ! ! ! !

List client names instead of check routing numbers.

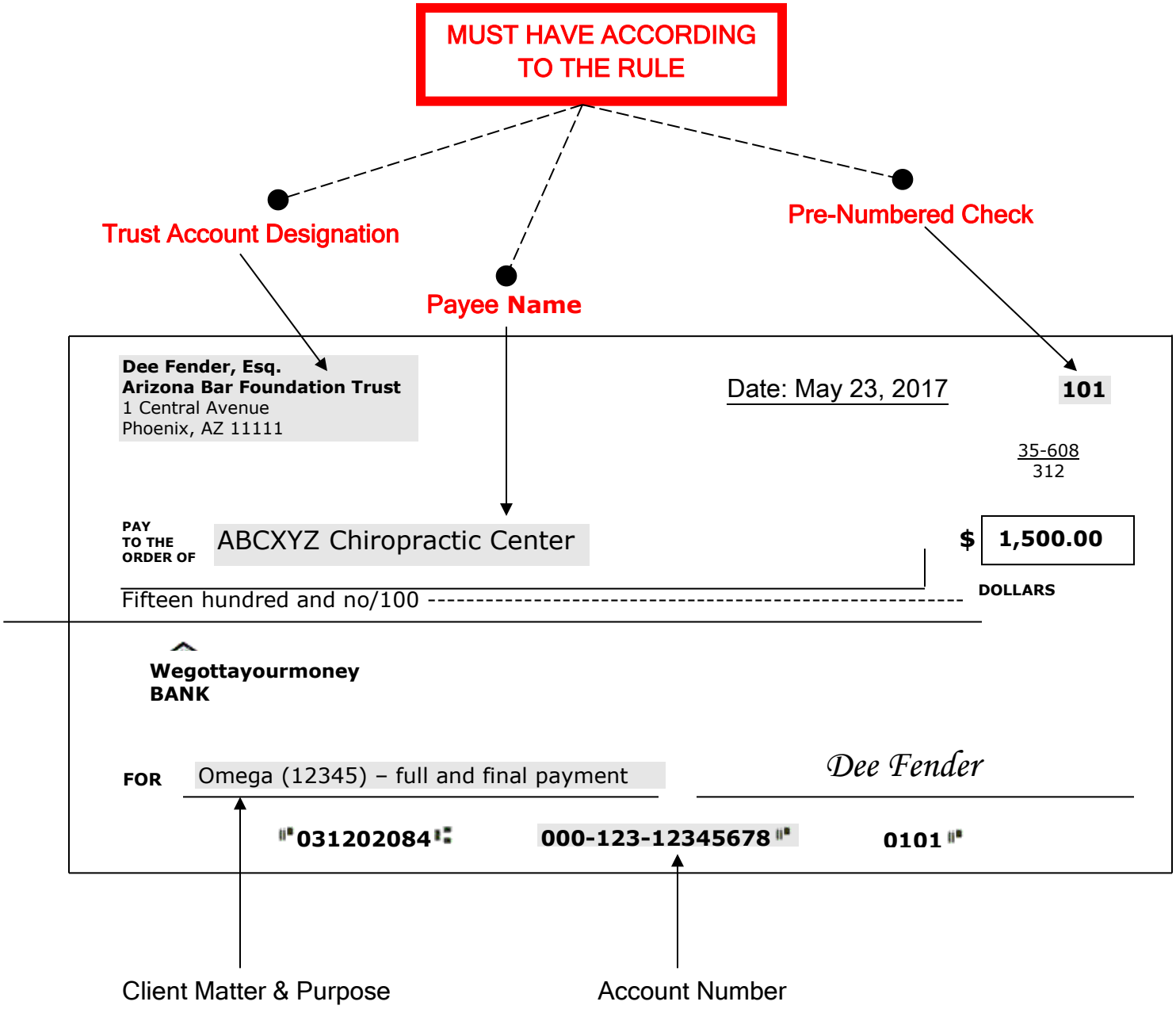
C. Deposit Log

Trust Account Deposit Log for: May 2013

Date of Deposit	Amount	Corresponding Client
05/01/2017	$5,000.00	Alpha, Alan
05/15/2017	$1,500.00	Beta, Betty
05/15/2017	$1,450.00	Gamma, George
05/15/2017	$5,100.00	Delta, David
05/15/2017	$2,000.00	Epsilon, Edward
05/16/2017	$10,000.00	Zeta, Zoe
05/16/2017	$8,000.00	Eta, Elise
05/19/2017	$3,700.00	Iota, Ingrid
05/20/2017	$500.00	Nu, Norman
05/20/2017	$7,500.00	Xi, Alexander
05/20/2017	$3,500.00	Omicron, Oliver
05/27/2017	$750.00	Pi, Patricia
05/27/2017	$750.00	Rho, Rosemary
05/29/2017	$1,500.00	Sigma, Sam
05/29/2017	$25,000.00	Tau, Theodore
05/29/2017	$10,000.00	Upsilon, Ursula
05/29/2017	$7,500.00	Phi, Peter
05/29/2017	$2,500.00	Lambda, Lisa
05/30/2017	$500.00	Mu, Matthew
05/30/2017	$1,500.00	Psi, Paul
05/30/2017	$8,000.00	Omega, Olivia

Total Deposit = $10,050.00 on 05/15/2017

D. Trust Account Check



E. Individual Client Ledger

Client: _____ Advance Fees

Matter: _____

Rec	Number	Date	Description of Transaction (Payor/Payee)	Disbursement	Deposit	Balance

Client: _____ Advanced Costs

Matter: _____

Rec	Number	Date	Description of Transaction (Payor/Payee)	Disbursement	Deposit	Balance

One Ledger for EACH Client per Matter

F. Administrative Funds/Bank Charges Ledger

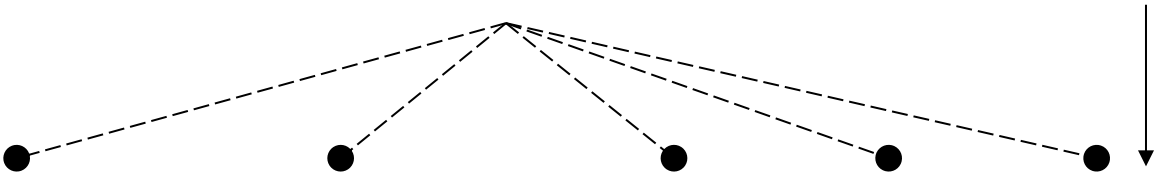
Rec	Number	Date	Description of Transaction (Payor/Payee)	Disbursement	Deposit	Balance
	DEP	12/01/16	Deposit to open account (Fender)		$50.00	$50.00
	Bank Fees	07/18/17	Epsilon returned deposit fee	$5.00		$45.00
	DEP	07/31/17	Epsilon reimbursement for $5 returned deposit bank charge		$5.00	$50.00
	Bank Charge	08/15/17	New check order charge	$24.95		$25.05

Create a ledger that shows how much money in the trust account belongs to you/firm that will pay miscellaneous bank fees and charges, and credit card fees.

G. General Ledger

MUST HAVE ACCORDING TO THE RULE

Always Calculate the Running Balance



Number	Date	Description of Transaction (Payor/Payee)	Disbursement	Deposit	Balance
DEP	12/01/16	Deposit to open acct – Fender Admin Funds		$50.00	$50.00
DEP	12/15/16	Gamma – advanced fee		$250.00	$300.00
1001	01/17/17	Dee Fender, Esq. – Gamma earned fees	$250.00		$50.00
DEP	02/01/17	Beta $1,500 fees and costs		$1,500.00	$1,550.00
1002	02/15/17	Superior Court – Nowhere County Filing Fee – Beta Cost	$125.00		$1,425.00
1003	02/15/17	Nowhere Vital Records – Birth Cert – Beta cost	$75.00		$1,350.00
1004	03/19/17	Dee Fender, Esq. – Beta earned fees	$600.00		$750.00
1005	04/19/17	Dee Fender, Esq. – Beta earned fees	$400.00		$350.00
DEP	05/02/17	Gamma $1,200 fees (earned upon receipt) $250 costs		$1,450.00	$1,800.00
1006	05/16/17	Record Round Up – Gamma costs	$150.00		$1,650.00
1007	05/16/17	Dee Fender, Esq. – Gamma earned fees	$1,200.00		$450.00
DEP	06/03/17	Delta $5,000 fees (earned upon receipt) $10,000 (unearned)		$15,000.00	$15,450.00
1008	06/17/17	Dee Fender, Esq. – Delta earned fees 8 hrs @ $250/hr	$2,000.00		$13,450.00
1009	06/17/17	Delta – refund of unused advanced fee	$13,000.00		$450.00
DEP	07/15/17	Epsilon $2,000 fees (unearned)		$2,000.00	$2,240.00
RTND DEP	07/18/17	Epsilon – returned deposited check for insufficient funds	$2,000.00		$450.00
BNK FEE	07/18/17	Epsilon Returned Deposit Fee	$5.00		$445.00
DEP	07/31/17	Epsilon $2,000 fees (unearned) with reimbursement for $5 returned deposit bank charge		$2,005.00	$2,450.00

H. Checkbook Register

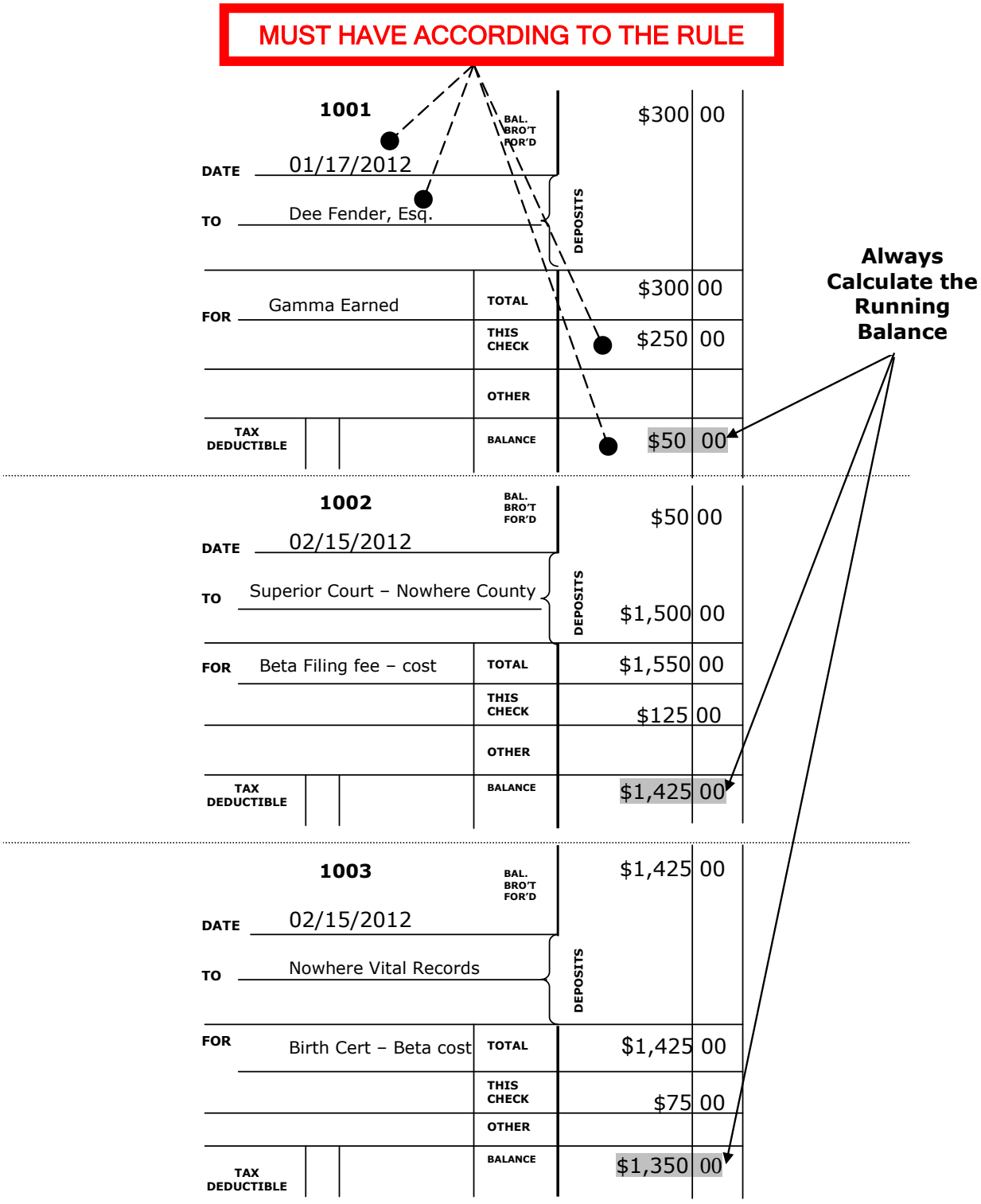
Always Calculate the Running Balance

MUST HAVE ACCORDING TO THE RULE

RECORD ALL DEBITS AND CREDITS THAT AFFECT YOUR ACCOUNT

CHECK NUMBER	DATE	DESCRIPTION OF TRANSACTION (Payor/Payee)	PAYMENT / DEBIT (-)		✓	FEE (-)	DEPOSIT / CREDIT (+)		BALANCE $	
DEP	12/01/16	Deposit to open acct – Fender Admin Funds					50	00	50	00
DEP	12/15/16	Gamma – advanced fee					250	00	300	00
1001	01/17/17	Dee Fender, Esq. – Gamma earned fees	250	00					50	00
DEP	02/01/17	Beta $1,500 fees and costs					1,500	00	1,550	00
1002	02/15/17	Superior Court – Nowhere County Filing Fee – Beta cost	125	00					1,425	00
1003	02/15/17	Nowhere Vital Records – Birth Cert – Beta cost	75	00					1,350	00
1004	03/19/17	Dee Fender, Esq. – Beta earned fees	600	00					750	00
1005	04/19/17	Dee Fender, Esq. – Beta earned fees	400	00					350	00
DEP	05/02/17	Gamma $1,200 fees (earned upon receipt) $250 costs					1,450	00	1,800	00
1006	05/16/17	Record Round Up – Gamma costs	150	00					1,650	00
1007	05/16/17	Dee Fender, Esq. – Gamma earned fees	1,200	00					450	00
DEP	06/03/17	Delta $5,000 fees (earned upon receipt) $10,000 (unearned)					15,000	00	15,450	00
1008	06/17/17	Dee Fender, Esq. - Delta earned fees 8 hrs @ $250/hr	2,000	00					13,450	00
1009	06/17/17	D. Delta – refund of unused advanced fee	13,000	00					450	00
DEP	07/15/17	Epsilon $2,000 fees (unearned)					2,000	00	2,450	00
RTND DEP	07/18/17	Epsilon – returned deposited check for insufficient funds	2,000	00					450	00
BNK FEE	07/18/17	Epsilon Returned Deposit Fee	5	00					445	00
DEP	07/31/17	Epsilon $2,000 fees (unearned) with reimbursement for $5 returned deposit bank charge					2,005	00	2,450	00

I. Three-Ring Trust Checkbook



J. Three-Way Reconciliation

As of the Month Ended
July 31, 2017

		BALANCE	
Client's Trust Ledger Balances:			
NAME OF CLIENT	**AMOUNT**		
Alpha	$2,005.00		
Beta	$300.00		
Gamma	$100.00		
Administrative Funds	$45.00		
TOTAL		$2,450.00	*
Balance per July 31, 2017 Trust Account Bank Statement		$520.00	
ADD: All Outstanding Deposits	$2,005.00		
LESS: All Outstanding Checks	$75.00		
ADJUSTED BALANCE		$2,450.00	*
Trust General Ledger/Checkbook Register Balance as of 07/31/2017		$2,450.00	*

* These amounts must match.

K. Sample Fee Agreement

To help you develop your own fee agreement, the State Bar's Lawyer Regulation Office, has drafted sample contingency, hourly and flat-fee fee agreements.

Use these as starting points for developing your own fee agreement because no one size fits all. The three sample fee agreements contain, however, some terms that are deemed necessary to all fee agreements.

Following the three standard sample fee agreements is a compilation of miscellaneous provisions that you may want to include in your own fee agreement. Whether to include any of them depends on your practice area and circumstances. These terms are optional but in many cases may be a "best practice" sort of provision. Modify them as you want and need.

We also provide a list of commonly used terms and phrases in fee agreements. We suggest that you review these terms when deciding which sample fee agreement is appropriate for your practice.

Reasonableness and the "look back"

Regardless of what you call your billing practice or how you will charge, your fee must always be reasonable and must always be disclosed to the client in writing. ER 1.5(a) and (b), Rule 42, Ariz. R. Sup. Ct.

At the end of the representation, the lawyer must perform a "look back" to determine whether the fees charged are reasonable based the factors listed in ER 1.5. Why? Our Supreme Court said in *In re Swartz*, 141 Ariz. 266, 686 P.2d 1236 (1984):

> [A] fee agreement between lawyer and client is not an ordinary business contract. The profession has both an obligation of public service and duties to clients which transcend ordinary business relationships and prohibit the lawyer from taking advantage of the client. Thus, in fixing and collecting fees the profession must remember that it is 'a branch of the administration of justice and not a mere money getting trade.'

141 Ariz. at 273, 686 P.2d at 1243 [internal citations omitted].

What factors determine whether a fee is reasonable?

ER 1.5(a) lists them:

(1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;
(2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;
(3) the fee customarily charged in the locality for similar legal services;
(4) the amount involved and the results obtained;
(5) the time limitations imposed by the client or by the circumstances;
(6) the nature and length of the professional relationship with the client;
(7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and
(8) the degree of risk assumed by the lawyer.

L. Types of Fees

Contingency fees

With a contingency fee, you establish a percentage you will take from any settlement authorized by the client, or recovery after a trial or appeal. The percentage may be different through certain milestones in a case. You cannot use contingency fee agreements in criminal cases or certain aspects of domestic relations matters. A contingency is permissible when the client agrees to pay a certain amount if a lawyer is successful on a certain outcome.

Where do I deposit the settlement check in a contingent-fee case?

Settlements or judgments belong to the client and must be deposited into the client trust account. Even if you are entitled to part of the settlement check, you must deposit it into the client trust account because some of the money does not belong to you.

When do I get my contingency fee?

Once you have prepared the settlement statement and provided it to the client and the check has cleared the issuing bank, you may withdraw your contingency fee from the client trust account -- unless the client contests the fee. If the client disputes your fee, you are only permitted to take that portion of your fee that is not at issue. You must leave the disputed portion of the fee in the client trust account until the dispute is resolved. If the entire fee is disputed, the entire fee must stay in the client trust account.

What is an unreasonable contingency fee?

There is no bright line. A contingency fee of more than 50 percent might be suspect because the lawyer has a greater interest in the outcome than the client. The actual amount of the fee should bear some relation to the work performed and risk taken. In addition, if the amount the lawyer takes as a fee is greater than the client's final recovery, there is a correspondingly greater risk that the lawyer's fee will be unreasonable. *See In re Swartz*, 141 Ariz. 266, 686 P.2d 1236 (1984).

Advanced Fees

An advanced fee is an amount paid to a lawyer in contemplation of future services that will be earned at an agreed-upon basis, whether hourly or flat. Any amount paid to a lawyer in contemplation of future services is an advanced fee regardless of what the fee is called. An advanced fee must be deposited into the client trust account.

Flat Fees

A flat fee is a fixed amount paid to a lawyer for specific, agreed-upon services, or for a fixed, agreed-upon stage in a representation, regardless of the time required of the lawyer to perform the service or reach the agreed-upon stage in the representation.

Where do I deposit a flat fee?

A flat fee may or may not be an advanced fee, but is not deemed earned until the work is performed. If a flat fee is not designated earned on receipt, then it is presumed to belong to the client and it must be deposited in the trust account. A flat fee is not an advance against the lawyer's hourly rate and may not be billed against at an hourly rate. If you are going to bill against a flat fee, then all of it must be deposited into your client trust account. If the fee is a flat fee that is deemed earned on receipt, it belongs to you and therefore should not be deposited into your client trust account.

When can I withdraw an advanced fee that is in my client trust account?

Whenever you bill for work actually done, you are entitled to withdraw that billed amount from your client trust account. Once you earn a portion and it becomes yours, it is improper to keep it in your trust account. If it is a flat fee that is not earned upon receipt, you can set up a schedule with your client regarding when the fee, or portions thereof, has been earned, and remove the earned amount from the client trust account.

How much of the flat fee do I get to keep?

If you have not completed the agreed-upon work, then you are only entitled to keep a portion of the flat fee. How much you get to keep should be determined by looking at what work was performed compared to what it was you promised to do. If the fee is a flat

fee that is deemed earned on receipt, you may be entitled to keep the entire fee if it is reasonable for the amount of work you have actually performed. Regardless of what type of fee you use, you can never keep a fee that has not been earned.

Billed fees

With billed fees, a lawyer takes no fee at the time representation, but instead bills the client after the work has been performed.

Where do I deposit billed fees?

Billed fees have been earned and therefore belong to you. They do not belong in the client trust account.

Retainer

A retainer is not for legal services and is not an advanced fee. It only secures your availability for the client. Few lawyers use a true retainer and instead require an advanced fee, which they mistakenly refer to as a "retainer."

Do I bill against a retainer?

No. It is earned on receipt.

Do I deposit the retainer in the client trust account?

No. It is your money.

What does a retainer require me to do?

You must make yourself available to perform work at the client's request, subject to any agreement you have made regarding when you will be available. You then bill for the work you do, but you do not bill against the retainer. Instead you will either bill the client or bill against any advanced fee you may have collected.

M. Explanation of Fee Agreement Terms

Earned on receipt

The designation "earned on receipt" tells the lawyer where the money received from the client must be deposited. It is not appropriate to designate funds as earned on receipt if the lawyer's true intention is to bill against the funds hourly, or to give the client a credit for a certain number of hours to be worked on the case in the future.

You should explicitly explain to the client the basis for using an earned-on-receipt fee. For example, if the fee is intended to compensate you for work that must be declined because of conflicts or time commitments, then the communication to the client should say so explicitly. Such statements must be true, of course. Merely reciting this language in a form agreement that bears no relationship to your workload or the likelihood of conflicts would violate ER 1.4.

If a fee is earned on receipt, are there any other requirements?

If you designate your fees as earned on receipt or nonrefundable, ER 1.5(d)(3) requires that you put in your fee agreement language that informs the client that the fee may still be refundable.

If a fee is earned on receipt, why should I have to refund any portion of it?

Even if a fee is designated as earned on receipt, you may have to promptly return any unused portion to your client. All fees, regardless of how they are classified, must be reasonable.

If a fee is earned on receipt, where do I deposit it?

You deposit earned-on-receipt fees in your operating account. They must not be placed in your client trust account as they are yours from the time you receive them.

If I may have to refund some of the fees, shouldn't I keep them in my trust account?

No, earned-on-receipt fees are your property and keeping them in the trust account would result in commingling and a violation of the Rules of Professional Conduct.

Non-refundable

What is a non-refundable fee?

Non-refundable refers to a fee agreement under which the lawyer may be entitled to the fee regardless of whether the lawyer actually performs the services called for in the agreement.

Is that an absolute?

No, although a non-refundable fee may be appropriate under certain circumstances, such as if the lawyer must reserve significant time to complete the service or must turn away other work, all fees must still be reasonable and are refundable if unearned. If you use this term, you must put in your fee agreement language that informs the client the fee may still be refundable.

Block billing

Block billing is the practice of lumping together multiple tasks without specifying how much time was spent on individual or discrete activities. It is discouraged because it is difficult to determine the reasonableness of the fees charged. *See Welch v. Metropolitan Life*, 480 F.3d 942 (9th Cir. 2007). It also does not provide the client with specific information about the work performed.

Minimum or incremental billing

Minimum or incremental billing is the practice of assigning a set minimum amount for a task, such as 0.2 (12 minutes) for phone calls, even though they may only take one minute. Lawyers are cautioned to analyze minimum billing at the end of a representation to make sure that the practice does not result in excessive billing. *See Welch v. Metropolitan Life*, 480 F.3d 942 (9th Cir. 2007).

All lawyers should also review the following:

ER 1.5 Fees
ER 1.15 Safekeeping Property (includes trust account provisions)
Rule 43, Arizona Rules of the Supreme Court (trust account rules)
Ariz. *Ethics Op.* 99-02
In re Connelly, 203 Ariz. 413, 55 P.3d 756 (2002)
In re Hirschfeld, 192 Ariz. 40, 960 P.2d 640 (1998)
In re Swartz, 141 Ariz. 266, 686 P.2d 1236 (1984)

N. Sample Contingent Fee Agreement

[LAW FIRM]CONTINGENT FEE AGREEMENT

SCOPE: _____ hires **[NAME/LAW FIRM]** to pursue claims he or she may have in connection with [INSERT DESCRIPTION OF REPRESENTATION OF WHAT YOU SPECIFICALLY ANTICIPATE DOING, INCLUDING WHEN THE REPRESENTATION STARTS AND WHEN THE REPRESENTATION CONCLUDES (e.g. DECREE IS ENTERED). ALSO INDICATE WHAT IS NOT INCLUDED IN THIS FEE AGREEMENT, (e.g. APPEAL, MISTRIAL, QUADRO AND IF FURTHER REPRESENTATION IS NEEDED AFTER THAT A SEPARATE FEE AGREEMENT WILL BE DRAFTED).

COSTS AND EXPENSES: You will be responsible for all actual out-of-pocket costs and expenses we incur on your behalf. Typical costs and expenses include: travel costs and expenses, long-distance telephone calls, outgoing fax (at INSERT RATE per page), Federal Express, courier services, and delivery charges, photocopying (at INSERT RATE per page), online database retrieval charges (Lexis, Westlaw, etc.), filing fees, wire transfers and other litigation related expenses. We anticipate making advances to cover out-of-pocket costs and expenses incurred but reserve the right to forward to you any larger items (such as expert witness fees or deposition costs and expenses) with the request that you pay them directly to the service providers. We will not incur costs and expenses in excess of $[XXX] on your behalf without first obtaining your consent. Costs and expenses advanced by us are taken out of your portion of any settlement proceeds after the contingency amount has been calculated.

FEE: You have retained us on a contingent fee basis and agree to pay us:

(1) Twenty-five (25) percent of the gross amount recovered by settlement prior to the filing of a complaint;
(2) Thirty-three and a third (33⅓) percent of the gross amount recovered by settlement after a complaint is filed but before a trial is commenced;
(3) Forty (40) percent of the gross amount recovered during or immediately after the first trial, by settlement or otherwise; or
(4) Forty-five (45) percent of the gross amount recovered if an appeal or further action is taken after the first trial.

For example, if the case settles for $100.00 prior to the filing of a complaint and you owe your health-care provider $10.00, we receive $25.00, the health-care provider receives $10.00, and you receive $65.00. If the case settles for $100.00 after the filing of a complaint and you owe your health-care provider $10.00, we receive $33.34, the health-care provider receives $10.00, and you receive $56.66.

Except as provided in the next paragraph, our fees will be payable only out of amounts recovered. If no recovery is obtained, no fees will be payable to us. You will, however, remain liable for all costs incurred on your behalf regardless of recovery.

TERMINATION OF REPRESENTATION AND POST-REPRESENTATION MATTERS: Either party may terminate the representation at any time, subject to our obligations under the Rules of Professional Conduct and the approval of the court if the matter is in litigation.

In the event this agreement is terminated by us before settlement or ultimate recovery, no contingent fees shall be payable to us, but you shall remain responsible for payment of all costs and expenses advanced by us.

In the event this agreement is terminated by you before settlement or ultimate recovery, and should you settle and recover funds after the termination of this agreement, you agree to pay us our fees at the hourly rates customarily charged by us for the time we reasonably spent on your behalf before your termination of this agreement, plus any costs and expenses advanced. Our hourly rate for lawyer [NAME] is $_____.

Unless previously terminated, our representation will terminate upon completion of the legal services described in this agreement.

CLIENT'S RESPONSIBILITIES: We cannot effectively represent you without your cooperation and assistance. You agree to cooperate fully with us and to promptly provide all information known or available to you that is relevant to the representation. Your obligations include timely providing requested information and documents, assisting in discovery, disclosure and trial preparation, cooperating in scheduling and related matters, responding timely to telephone calls and correspondence, and informing us of changes in your address, telephone numbers and e-mail address. It is important that you retain all communications from and to us, including e-mails and attachments to e-mails.

SETTLEMENT: We will not enter into a settlement without your consent.

DISBURSEMENTS: The Ethical Rules place certain limitations upon the disbursement of funds from client trust accounts. In some cases, this may require us to wait 10 business days after depositing a financial instrument before disbursing the funds to you or a third party.

DOCUMENT RETENTION: At the end of our engagement, we will turn over the hard copy or electronic version of the file to you. If you do not want the file, you agree that the file may be destroyed in accordance with our document retention policy. Currently, it is our policy to destroy files five years after the termination of the representation.

[NOTE TO LAWYER: You may need to modify the retention term depending on the type of representation and whether you have accepted original documents from the client. *See* Ariz. *Ethics Op.* 08-02]

ARBITRATION OF FEE DISPUTES: If a dispute arises between us and you regarding our fees, the parties agree to resolve that dispute through the State Bar's Fee Arbitration Program. Either party may initiate fee arbitration by contacting the State Bar's Fee Arbitration Coordinator at 602.340.7379.

NO ADVICE REGARDING THIS FEE AGREEMENT: We are not acting as your counsel with respect to this agreement. If you wish to be advised on whether you should enter into this agreement, we recommend that you consult with independent counsel of your choice.

NO GUARANTEES HAVE BEEN MADE AS TO WHAT AMOUNTS, IF ANY, YOU MAY BE ENTITLED TO RECOVER IN THIS CASE OR THE FINAL OUTCOME IN THIS CASE.

DATED this ___day of _____, 20__. _____
Client's Name

DATED this __day of _____, 20__. _____
Lawyer's Name

O. Sample Hourly Fee Agreement

[LAW FIRM] HOURLY FEE AGREEMENT

SCOPE: _____ hires **[NAME/LAW FIRM]** to pursue claims he or she may have in connection with [INSERT DESCRIPTION OF REPRESENTATION OF WHAT YOU SPECIFICALLY ANTICIPATE DOING, INCLUDING WHEN THE REPRESENTATION STARTS AND WHEN THE REPRESENTATION CONCLUDES (e.g. DECREE IS ENTERED). ALSO INDICATE WHAT IS NOT INCLUDED IN THIS FEE AGREEMENT, (e.g. APPEAL, MISTRIAL, QUADRO AND IF FURTHER REPRESENTATION IS NEEDED AFTER THAT A SEPARATE FEE AGREEMENT WILL BE DRAFTED).

HOURLY FEE: You have retained us on an hourly basis. We will bill for lawyer services at a rate of $_____ per hour for [NAME OF LAWYER]. Other lawyers and non-lawyer professionals may also work on your case. These other individuals will bill in accordance with the hourly rates set forth in the attached Schedule A, which is hereby incorporated into this agreement.

It is impossible to determine in advance how much time will be needed to handle your case. Any figures quoted to you for the total cost of our services are merely estimates. The opposing party, or others, may engage in activities beyond our control that require an expenditure of time not originally contemplated.

COSTS AND EXPENSES: You agree to pay for all actual out-of-pocket costs and expenses we incur on your behalf. Typical costs and expenses include: filing fees, service of process, depositions, expert witness fees, travel costs and expenses, long-distance telephone calls, outgoing fax (at INSERT RATE per page), Federal Express, courier services, and delivery charges, photocopying (at INSERT RATE per page), wire transfers and online database retrieval charges (Lexis, Westlaw, etc.).

We may elect to cover certain out-of-pocket costs and expenses on your behalf, but we reserve the right to seek reimbursement from you. You agree to reimburse us for such out-of-pocket costs and expenses. We will not incur costs and expenses in excess of $_____ on your behalf without first obtaining your consent.

ADVANCED DEPOSIT(S): You agree to pay an advanced deposit of $_____ for fees, costs and expenses. The advanced deposit(s) will be deposited into our client trust account. We will deduct fees, costs and expenses from the advanced deposit(s) as fees are earned or costs and expenses are incurred. We may require an additional advanced deposit of fees or costs and expenses. We will refund to you any balance of the advanced deposit(s) remaining after the representation has concluded.

BILLING: We will bill you on a monthly basis for services performed in the preceding month. The monthly statement will identify the services performed, the fees charged for those services, and costs and expenses incurred. The statement also will identify the balance of any advanced deposit(s) remaining after fees, costs and expenses set forth in the statement have been deducted. If your advanced deposit(s) has been depleted, you are expected to remit payment within 30 days of the date of the statement.

CLIENT'S RESPONSIBILITIES: We cannot effectively represent you without your cooperation and assistance. You agree to cooperate fully with us and to promptly provide all information known or available to us that is relevant to the representation. Your obligations include timely providing requested information and documents, assisting in discovery, disclosure and trial preparation, cooperating in scheduling and related matters, responding timely to telephone calls and correspondence, and informing us of changes in your address, telephone numbers and e-mail address. It is important that you retain all communications from and to us, including e-mails and attachments to e-mails.

SETTLEMENT: We will not enter into a settlement without your consent.

DISBURSEMENTS: The Ethical Rules place certain limitations upon the disbursement of funds from client trust accounts. In some cases, this may require us to wait 10 business days after depositing a financial instrument before disbursing the funds to you or a third party.

TERMINATION OF REPRESENTATION AND POST-REPRESENTATION MATTERS: Either party may terminate the representation at any time, subject to our obligations under the Rules of Professional Conduct and the approval of the court if the matter is in litigation.

Unless previously terminated, our representation will terminate upon completion of the legal services described in this agreement. You are engaging us to provide legal services in connection with the specific matter identified in this agreement. Unless you retain us to provide additional advice or services, you understand we have no continuing obligation to represent you.

DOCUMENT RETENTION: At the end of the representation, we will turn over the hard copy or electronic version of the file to you. If you do not want the file, you agree the file may be destroyed in accordance with our document retention policy. Currently, it is our policy to destroy files five years after the termination of the representation.

> [NOTE TO LAWYER: You may need to modify the retention term depending on the type of representation and whether you have accepted original documents from the client. *See* Ariz. *Ethics Op.* 08-02]

ARBITRATION OF FEE DISPUTES: If a dispute arises between you and us regarding our fees, the parties agree to resolve that dispute through the State Bar's Fee Arbitration

Program. Either party may initiate fee arbitration by contacting the State Bar's Fee Arbitration Coordinator at 602.340.7379.

NO ADVICE REGARDING THIS FEE AGREEMENT: We are not acting as your counsel with respect to this agreement. If you wish to be advised on whether you should enter into this agreement, we recommend you consult with independent counsel of your choice.

NO GUARANTEES HAVE BEEN MADE AS TO THE FINAL OUTCOME IN YOUR LEGAL MATTER.

DATED this ___day of _____, 20__. _____
Client's Name

DATED this __day of _____, 20__. _____
Lawyer's Name

P. Sample Flat Fee Agreement

[LAW FIRM] FLAT FEE AGREEMENT

SCOPE: _____ hires **[NAME/LAW FIRM]** to pursue claims he or she may have in connection with [INSERT DESCRIPTION OF REPRESENTATION OF WHAT YOU SPECIFICALLY ANTICIPATE DOING, INCLUDING WHEN THE REPRESENTATION STARTS AND WHEN THE REPRESENTATION CONCLUDES (e.g. DECREE IS ENTERED). ALSO INDICATE WHAT IS NOT INCLUDED IN THIS FEE AGREEMENT, (e.g. APPEAL, MISTRIAL, QUADRO AND IF FURTHER REPRESENTATION IS NEEDED AFTER THAT A SEPARATE FEE AGREEMENT WILL BE DRAFTED).

FLAT FEE: You have retained us on a flat fee basis. You will pay us $_____ as the entire fee for the representation described in this agreement. This fee is earned-on-receipt, and will not be deposited into our client trust account.

COSTS AND EXPENSES: You agree to pay for all actual out-of-pocket costs and expenses we incur on your behalf. Typical costs and expenses include: filing fees, service of process, depositions, expert witness fees, travel costs and expenses, long-distance telephone calls, outgoing fax (at INSERT RATE per page), Federal Express, courier services, and delivery charges, photocopying (at INSERT RATE per page), wire transfers, and online database retrieval charges (Lexis, Westlaw, etc.).

We may elect to cover certain out-of-pocket costs and expenses on your behalf, but we reserve the right to seek reimbursement from you. You agree to reimburse us for such out-of-pocket costs and expenses. We will not incur costs and expenses in excess of $_____on your behalf without first obtaining your consent.

> [NOTE TO LAWYER: You should determine whether this cost language is appropriate. If costs are already included as part of the flat-fee payment, then this language should be modified accordingly.]

TERMINATION OF REPRESENTATION AND POST-REPRESENTATION MATTERS: Either party may terminate the representation at any time, subject to our obligations under the Rules of Professional Conduct and the approval of the court if the matter is in litigation.

Unless previously terminated, our representation will terminate upon completion of the legal services described in this agreement. You understand we have no continuing obligation to represent you unless you retain us to provide additional advice or services.

REFUND: If you terminate the representation before we have provided all legal services described in this agreement, you may be entitled to a refund of all or part of the flat fee based on the value of the legal services performed prior to termination.

CLIENT'S RESPONSIBILITIES: We cannot effectively represent you without your cooperation and assistance. You agree to cooperate fully with us and to promptly provide all information known or available to you that is relevant to our representation. Your obligations include timely providing requested information and documents, assisting in discovery, disclosure and trial preparation,

cooperating in scheduling and related matters, responding timely to telephone calls and correspondence, and informing us of changes in your address, telephone numbers and e-mail address. It is important that you retain all communications from and to us, including e-mails and attachments to e-mails.

SETTLEMENT: We will not enter into a settlement without your consent.

DISBURSEMENTS: The Ethical Rules place certain limitations upon the disbursement of funds from client trust accounts. In some cases, this may require us to wait 10 business days after depositing a financial instrument before disbursing the funds to you or a third party.

DOCUMENT RETENTION: At the end of the representation, we will turn over the hard copy or electronic version of the file to you. If you do not want the file, you agree the file may be destroyed in accordance with our document retention policy. Currently, it is our policy to destroy files five years after the termination of the representation.

> NOTE TO LAWYER: You may need to modify the retention term depending on the type of representation and whether you have accepted original documents from the client. *See* Ariz. *Ethics Op.* 08-02]

ARBITRATION OF FEE DISPUTES: If a dispute arises between you and us regarding our fees, the parties agree to resolve that dispute through the State Bar's Fee Arbitration Program. Either party may initiate fee arbitration by contacting the State Bar's Fee Arbitration Coordinator at 602.340.7379.

NO ADVICE REGARDING THIS FEE AGREEMENT: We are not acting as your counsel with respect to this agreement. If you wish to be advised on whether you should enter into this agreement, we recommend you consult with independent counsel of your choice.

NO GUARANTEES HAVE BEEN MADE AS TO THE FINAL OUTCOME IN YOUR LEGAL MATTER.

DATED this ___day of _____, 20__. _____
Client's Name

DATED this ___day of _____, 20__. _____
Lawyer's Name

Q. Sample Flat Fee and Hourly Agreement

[LAW FIRM] FLAT FEE AND HOURLY AGREEMENT

SCOPE: _____ hires **[NAME/LAW FIRM]** to pursue claims he or she may have in connection with the _____ matter more particularly described as follows: [INSERT DESCRIPTION OF REPRESENTATION OF WHAT YOU SPECIFICALLY ANTICIPATE DOING FOR THE FLAT FEE BELOW, INCLUDING WHEN THE REPRESENTATION STARTS AND WHEN THE REPRESENTATION CONCLUDES (e.g. DECREE IS ENTERED). ALSO INDICATE WHAT IS NOT INCLUDED IN THIS FEE AGREEMENT, (e.g. APPEAL, MISTRIAL, QUADRO).

FLAT FEE: You have hired us on a flat fee and hourly basis. You will pay us $_____ as the flat fee portion for the representation described in the SCOPE section of this fee agreement, above. This fee is earned-on-receipt, and will not be deposited into our client trust account.

REFUND OF FLAT FEE: If you terminate the representation before we have provided all legal services described in this agreement, you may be entitled to a refund of all or part of the flat fee based on the value of the legal services performed prior to termination.

HOURLY FEE: You have also hired us on an hourly basis. Following your use of those services specifically described in the SCOPE above, we will bill for lawyer services at a rate of $_____ per hour for any additional services, identified in the attached Schedule B. Any additional services must be different than those listed in the SCOPE section of this agreement and we will begin providing additional services only after fully consulting with you and obtaining your informed consent that we may proceed with the additional services. Other lawyers and non-lawyer professionals may also work on your case. These other individuals will bill in accordance with the hourly rates set forth in the attached Schedule A, which is hereby incorporated into this agreement.

It is impossible to determine in advance how much time will be needed to handle your case. Any figures quoted to you for the total cost of our services are merely estimates. The opposing party, or others, may engage in activities beyond our control that require an expenditure of time not originally contemplated.

Neither the flat fee nor the hourly fee includes costs and expenses which must be paid or reimbursed separately.

[SCHEDULE B WILL NOT EXIST UNTIL AFTER CONSULTATION WITH THE CLIENT AND THE SPECIFICS OF ANY ADDITIONAL SERVICES ARE IDENTIFIED TO THE CLIENT. SCHEDULE B SHOULD INCLUDE A SIGNATURE LINE FOR THE CLIENT THAT THEY HAVE BEEN CONSULTED, REVIEWED THE SCHEDULE AND APPROVE THE ADDITIONAL SERVICES TO BE RENDERED AT AN HOURLY BASIS.]

COSTS AND EXPENSES: You agree to pay for all actual out-of-pocket costs and expenses we incur on your behalf. Typical costs and expenses include: filing fees, service of process, depositions, expert witness fees, travel costs and expenses, long-distance telephone calls, outgoing

fax (at XXX per page), Federal Express, courier services, and delivery charges, photocopying (at XXX per page), wire transfers and online database retrieval charges (Lexis, Westlaw, etc.).

We may elect to cover certain out-of-pocket costs and expenses on your behalf, but we reserve the right to seek reimbursement from you. You agree to reimburse us for such out-of-pocket costs and expenses. We will not incur costs and expenses in excess of [$XXX] on your behalf without first obtaining your consent.

TERMINATION OF REPRESENTATION AND POST-REPRESENTATION MATTERS: Either party may terminate the representation at any time, subject to our obligations under the Rules of Professional Conduct and the approval of the court if the matter is in litigation.

Unless previously terminated, our representation will terminate upon completion of the legal services described in this agreement. You understand we have no continuing obligation to represent you unless you hire us to provide additional advice or services.

CLIENT'S RESPONSIBILITIES: We cannot effectively represent you without your cooperation and assistance. You agree to cooperate fully with us and to promptly provide all information known or available to you that is relevant to the representation. Your obligations include timely providing requested information and documents, assisting in discovery, disclosure and trial preparation, cooperating in scheduling and related matters, responding timely to telephone calls and correspondence, and informing us of changes in your address, telephone numbers and e-mail address. It is important that you retain all communications from and to us, including e-mails and attachments to e-mails.

SETTLEMENT: We will not enter into a settlement without your consent.

DISBURSEMENTS: The Ethical Rules place certain limitations upon the disbursement of funds from client trust accounts. In some cases, this may require us to wait 10 business days after depositing a financial instrument before disbursing the funds to you or a third party.

DOCUMENT RETENTION: At the end of the representation, we will turn over the file (hard copy or electronic) to you. If you do not want the file, you agree the file may be destroyed in accordance with our document retention policy. Currently, it is our policy to destroy files five years after the termination of the representation.

> [NOTE TO LAWYER: You may need to modify the retention term depending on the type of representation and whether you have accepted original documents from the client. *See* Ariz. *Ethics Op.* 08-02]

ARBITRATION OF FEE DISPUTES: If a dispute arises between you and us regarding our fees, the parties agree to resolve the dispute through the State Bar's Fee Arbitration Program. Either party may initiate fee arbitration by contacting the State Bar's Fee Arbitration Coordinator at 602.340.7379.

NO ADVICE REGARDING THIS FEE AGREEMENT: We are not acting as your counsel with respect to this agreement. If you wish to be advised on whether you should enter into this agreement, we recommend you consult with independent counsel of your choice.

NO GUARANTEES HAVE BEEN MADE AS TO THE FINAL OUTCOME IN YOUR LEGAL MATTER.

DATED this ___day of _____, 20__. _____
Client's Name

DATED this ___day of _____, 20__. _____
Lawyer's Name

R. Sample Miscellaneous Fee Agreement Provisions

Instructions: The following provisions are additional terms that may not be included in the above fee agreement samples. A lawyer may need or wish to add one or more of these specific terms to the fee agreement depending on the specific circumstances of the case and the nature of the representation and fee agreement.

- Arizona Discovery Rules

Arizona's discovery rules are comprehensive and substantially different from how discovery is conducted in other states. The rules encourage early Court involvement in case management, require disclosures by the parties and contain presumptive discovery limits. The rules require clients and their lawyers to conduct a reasonable inquiry and investigation about all matters to be revealed in the disclosure statement. We have the duty to investigate facts that are good and bad for you. The failure of you or us to conduct a reasonable inquiry and investigation into these topics and to disclose all relevant information may subject you, or us, or both to sanctions. Furthermore, any evidence favorable to you that is not timely disclosed in accordance with the rules cannot be used at trial.

- Business Transaction with Client

This representation involves a business, property or financial transaction between the lawyer and the client. The terms of the transaction as well as all elements necessary to comply with the Rules of Professional Conduct (ER 1.8(a)) are contained in a separate writing attached hereto and signed by you.

- Client Files and File Maintenance

During the time we represent you, we will maintain a file relating to your legal matter. At the conclusion of the representation, we will give your file to you. After we give your file to you, information contained in your file will no longer be available through our firm. Take measures to protect your file. If we are unable to return your file to you at the conclusion of the representation, we will maintain your file for five years after representation ends. By signing this fee agreement you agree that your file may be destroyed after that five-year period ends.

[We maintain records electronically and by use of digital images and do not retain paper copies of documents, unless required by rule or statute. You may obtain paper copies of documents in your file upon request to us, with reasonable notice. By signing this fee agreement, you consent to us maintaining your file electronically.]

> [NOTE TO LAWYER: Refer to Ariz. Ethics Ops. 08-02 and 07-02 for a more complete discussion of these issues.]

- Communications

We will make every attempt to return all phone calls within 24 hours. We encourage e-mail communications as well. Non-lawyer staff may be directed to communicate with you, if appropriate. We will not communicate confidential information about the representation to third persons, including your family members, unless you specifically direct us to do so. We will send you copies of all relevant documents and correspondence that we receive in the case so that you can maintain a file of the legal matter. All communication with you will be billed for in accordance with the terms of the fee agreement.

> [NOTE TO LAWYER: You should update this clause with the specifics of your firm's communications policy.]

- Conflict of Interest

This representation presents a conflict of interest under the Ethical Rules. However, we believe that we will be able to provide competent and diligent representation to each affected client. We have provided a separate writing describing the nature of the conflict and the risks inherent in proceeding with the representation, as well as reasonably available alternatives. By signing that separate writing explaining the conflict, you agree to the continuation of the representation and waive the conflict described therein.

> [NOTE TO LAWYER: There are some conflicts that your client may not consent to. You are responsible for determining whether you must obtain your client's informed consent pursuant to ER 1.7(b). Additionally, please remember that you cannot ask a client to prospectively consent to a future conflict that is not yet identified. See ER 1.0(e)..]

- Disputed Funds

If we possess funds in which you and someone else have a claim or interest, we must hold the funds in our client trust account until the dispute is resolved. We will promptly disburse, however, any portion of the funds not in dispute. We will not unilaterally assume to arbitrate a dispute between you and a third party and we may have to file an action to have a court resolve the dispute.

We will send you monthly billing statements for costs, disbursements and expenses incurred in connection with this matter. The statements shall include the amount, rate, and basis of calculation or other method of determination of fees and costs and expenses. Each statement is to be paid in full or disputed within [xx days] after the date of such statement.

- Earned-on-Receipt Fee

This fee is earned-on-receipt and will not be billed against on an hourly basis. It will not be deposited into our client trust account, but will be deposited into our general operating account. Even though the fee is earned-on-receipt, you may nevertheless discharge us at any time and in that event may be entitled to a refund of all or part of the fee based upon the value of the representation.

- Electronic Communications

We communicate from time to time with our clients via facsimile, mobile telephone, and e-mail. No form of communication is completely secure and these forms of communication have some risk of improper interception even though we maintain reasonable security measures to assure the confidentiality of your information. We retain many file documents in electronic format only and these may be stored on a separate third party server. Accordingly, unless you instruct us that you prefer to receive only a paper copy in the mail and do not wish to communicate by e-mail, we will send you each document that is relevant to your case by e-mail as a scanned document in "pdf' or "tif' format. You are responsible for providing us with an e-mail address that you want us to use for correspondence related to the representation. You should check that e-mail address regularly. We will assume that third parties (e.g., employers or family members) do not have access to that e-mail address so you can receive confidential correspondence from us at that address. We also will assume that you are receiving and reviewing our e-mails at that address unless you alert us to an issue. Please be certain that your e-mail filters do not block e-mails from our office and that the allowable size of incoming e-mails is sufficient to accept e-mails from us with attachments.

- Fee Shifting

The matter for which you have hired us is one in which lawyers' fees may be recovered by one party from the other. Regardless whether fees are awarded, you are responsible for all fees owing under the terms of this fee agreement. If appropriate, we will press a claim asking the Court to award your fees incurred in this matter. Please also understand that the other party may attempt to shift their fees to you. Moreover, the provisions under which a Court may shift fees generally leaves that decision to the discretion of the Court to decide whether, and in what amount, to award fees.

- Interest Charges

If a billing statement is not paid when due or disputed within [xx days] after the date of such statement, interest will be charged on the principal balance (fees, costs and expenses) shown on the statement. Interest will be calculated by multiplying the unpaid

balance by the periodic rate of .xxx% per month (XX PERCENT [xx%] ANNUAL PERCENTAGE RATE). The unpaid balance will bear interest until paid.

- Joint Representation (two or more clients)

We are representing both you _____ and _____ in the same or a related matter. At this time, such representation is permitted because there does not appear to be a conflict of interest between the parties. This may change and a conflict may arise at some later point in the representation. We will continue to evaluate the case and the existence of any possible conflicts of interest. Should a conflict arise, we will advise all affected clients and comply with the requirements of Ethical Rule 1.7, which may include withdrawal. In addition, all parties agree and provide their consent that we may discuss the case with one or all of you, together or apart, and that we will not keep information confidential between the parties while jointly representing you.

> [NOTE TO LAWYER: You must discuss with your clients and should clearly articulate prior to or within a reasonable time after beginning your joint representation which client will get the original file and which will be given a copy of the original file at the conclusion of the representation. See ER 1.16(d), comment 9.]

- Limited Scope Representation

LIMITED SCOPE: _____ hires [NAME/LAW FIRM] to pursue claims he or she may have in connection with [INSERT DESCRIPTION OF REPRESENTATION OF WHAT YOU SPECIFICALLY ANTICIPATE DOING, INCLUDING WHEN THE REPRESENTATION STARTS AND WHEN THE REPRESENTATION CONCLUDES (e.g. DECREE IS ENTERED). ALSO INDICATE WHAT IS NOT INCLUDED IN THIS FEE AGREEMENT, (e.g. APPEAL, MISTRIAL, QUADRO AND IF FURTHER REPRESENTATION IS NEEDED AFTER THAT A SEPARATE FEE AGREEMENT WILL BE DRAFTED).

You are agreeing that the scope of this representation is limited as follows:

Notwithstanding anything to the contrary in this agreement, this representation is terminated when the services listed in this document have been completed, and you will not expect any further services to be performed, including document-drafting, giving legal advice, or court appearances, unless you sign a new fee agreement with this firm.

Unless the opposing party or attorney knows of this firm's representation, you are considered to be unrepresented; you will be expected to communicate with the opposing party or attorney as though you do not have a lawyer representing you.

[OR]

We will inform the opposing party or attorney of the limited scope representation, and we will instruct them as to when they may communicate directly with you. These instructions will include which of us to contact concerning specific matters, to whom and where they should send pleadings, correspondence and other notices, and whether you have authorized us to accept service on your behalf.

If this matter involves litigation, we will notify the Court that we have agreed to provide you with limited scope representation, specifying the matters, hearings or issues on which we will represent you. When we have completed the representation, we will withdraw from the action with your consent, and we will surrender all documents and property to which you are entitled, and all documents reflecting work done for you. We will provide your contact information, including your address, telephone number, and e-mail address to the Court and the other parties.

You agree not to unreasonably withhold your consent to our withdrawal or make it subject to any conditions.

At the end of the representation, we anticipate that the status of the matter will be as follows:

_____. We will inform you of any outstanding deadlines at that time. Unless you get another lawyer to represent you, you will be responsible for representing yourself. This includes communicating with the opposing attorney, but if the party is unrepresented, then with the party directly. This also includes appearing at all court hearings and filing whatever documents are appropriate within the timeframes specified by statute, order or rule, and sending copies to the opposing party or their lawyer.

- Local Counsel in Pro Hac Vice Matter

Our role in this matter is to serve as local counsel for an out-of-state firm. The out-of-state firm will have principal responsibility for the litigation. While we will attempt to avoid undue costs and expenses caused by having two firms duplicate their efforts, we are required by the ethical rules to conduct a reasonable inquiry to ensure that pleadings and filings are well grounded in fact and law and otherwise meet the applicable standards. Accordingly, although we understand and will seek to accommodate your interest in avoiding duplicate legal fees, our professional obligations compel us to undertake activities and investigations deemed necessary to discharge these obligations.

- Miscellaneous Bank Fees and Merchant Fees or Credit Card Transaction Fees

We/You agree to pay merchant fees or credit card transaction fees incurred on your behalf. Merchant fees and credit card transaction fees are deducted from the amount of the credit card charge to pay the company that issued your credit card, the lawyer or law firm's credit card processing service, the credit card association (e.g. Visa, MasterCard) and related charges. The [gross/net] amount of the credit card payment will be credited to your account.

We/You agree to pay bank fees incurred on your behalf. Typical bank fees include, but are not limited to: returned deposit fees, electronic transfer fees, stop payment fees, wire fees, and copy charges. The amount of the bank fee incurred will either be deducted from your current trust account balance or included on your billing statement.

- Outside Lawyers/Law Firms

Should it become advisable to associate with another lawyer or law firm to assist in the representation, we will advise you immediately in writing. We will only associate with outside counsel if you agree, in writing, to the participation of each lawyer/law firm. We will identify each lawyer or law firm who we believe should participate in the representation and they will assume joint responsibility for the representation. We assure you, with or without associating with another lawyer or law firm, the total fee will be reasonable.

- Property for Services

This representation involves the exchange of your property (or services) for legal services or the securing of a legal fee via lien or encumbrance of your property. The terms of the transaction as well as all elements necessary to comply with the Rules of Professional Conduct (ER 1.8(a)) are contained in a separate writing attached hereto and signed by you.

- Third Party Payor

Your legal fees are being paid by a third party. Both you and the third party must understand that our ethical duties of confidentiality and communications are owed to you, not to the person paying the fees. All decisions regarding the legal status and strategy of your case shall be discussed only with you unless you give express written permission. Any refund shall be returned to the party who provided the funds.

> [NOTE TO LAWYER: You should determine whether a third party payor situation creates a conflict of interest that would require

compliance with ER 1.7(b) and securing your client's informed consent in writing, if the conflict can be waived. See, ER 1.8(f).]

- True Retainer

You agree to pay the retainer in the amount of $_____. This retainer serves merely to ensure our availability to represent you and to preclude us from taking adverse representation. This retainer DOES NOT cover any legal services to be provided. Legal fees will be charged separately under the terms of the agreement.

- Trust Account Deposits and Payment of Interest

Interest earned on any funds that we receive from you or on your behalf that are deposited to our IOLTA (Interest on Lawyer Trust Account) will be paid directly by the financial institution or investment company to the Arizona Foundation for Legal Services and Education pursuant to Rule 43, Ariz. R. Sup. Ct. The Foundation uses the interest or dividends to support programs to assist in the delivery of legal services to the poor, for law-related education programs, to fund studies or programs designed to improve the administration of justice, to maintain a reasonable reserve and to pay administrative costs.

- Use of Associate Lawyer

I will be the lawyer ultimately responsible in connection with the representation; however, I may call upon other lawyers and personnel in our office for a variety of reasons to the extent necessary to assist me. A list of the firm lawyers and personnel, and their respective rates, is attached to this agreement.

S. Notice to Financial Institution

(ATTORNEY: Please complete this form and submit it to your financial institution.)

.....

Arizona Foundation for LEGAL SERVICES & EDUCATION

The Arizona IOLTA Program is administered by the Arizona Foundation for Legal Services & Education.

NOTIFICATION TO IOLTA APPROVED FINANCIAL INSTITUTION
regarding an Arizona IOLTA account

TO: _____ _____
(Bank) (Branch)

The undersigned is a participant in the interest-bearing trust account program mandated by Rule 43 of the Rules of the Supreme Court of Arizona. Under this program, the undersigned's law firm's trust account

_____ _____
(Account Number) (Account Name)

should be placed in an interest-bearing account under the **Tax ID No. 95-3351710** and should be identified with the words "**AZ IOLTA**" or "**AZ Trust**" following the attorney or firm name in the title of the account.

The Arizona Foundation for Legal Services & Education has previously provided your institution with the guidelines for the program and report forms that you are to complete and file with the Foundation. These are available also at www.azflse.org/azflse/IOLTA/infoforbanks.cfm. Please provide the undersigned law firm with a copy of the report submitted to the Foundation or a regular monthly statement. No form 1099 is to be filed with the IRS.

Appendix B-11

The undersigned authorizes the disclosure of this account information to the Arizona IOLTA program.

_____ _____
(Signature) (State Bar Number)

_____ _____
(Print Name) (Date)

AZFLSE – 4201 N. 24th St. Suite 210 Phoenix, AZ 85016 – 602-340-7260

INSTRUCTIONS FOR OPENING A NEW IOLTA ACCOUNT

Supreme Court Rule 43 establishes Arizona's mandatory Interest on Lawyers' Trust Accounts program (IOLTA). Rule 43 requires all attorneys who receive client funds in Arizona, or in connection with representation of clients in Arizona, to maintain an interest bearing trust account to pool client funds of minimal amounts.

If you are joining a law firm that already has an active IOLTA account which you will use, no further action is needed at this time. You will only need to report your firm's IOLTA account information on your next State Bar dues statement.

If you are opening a new IOLTA account for which you will be the responsible party:

a) Complete the "Notification to Financial Institution" and submit it to your financial institution to make certain the financial institution assigns the account the Foundation's tax identification number, 95-3351710, and not your own, and that it understands that the interest is to be paid to the Arizona Foundation for Legal Services & Education for IOLTA; and

b) Complete the "Arizona IOLTA Enrollment/Change" form and submit it to the Arizona Foundation for Legal Services & Education.

Any time a change is made to your IOLTA account status (opening a new account, closing an old account), the change must be reported to the IOLTA program with the "Arizona IOLTA Enrollment/Change Form."

If you think you may be exempt from holding an IOLTA account but aren't sure, please contact the confidential Trust Account Hotline at the State Bar at 602-340-7305.

If you need help setting up your IOLTA account, please call a Practice Management Advisor in the Law Office Management Assistance Program (LOMAP) department of the State Bar at 602-340-7332.

Arizona Foundation for LEGAL SERVICES & EDUCATION

To be used for a NEW IOLTA or to UPDATE an Existing IOLTA.

ARIZONA ATTORNEY IOLTA ENROLLMENT / CHANGE FORM

☐ I am a signer I responsible party for the following new IOLTA account:

Name of financial institution: _____

Name of branch office: _____

Mailing address of branch office: _____

City, State, ZIP: _____

Name on the account: _____

Account number: _____

Date the account was established: _____

☐ I closed an IOLTA account:

Name of financial institution: _____

Account number: _____

Date the account was closed: _____

_____ (Your State Bar Membership No.)

_____ (Your Signature)

_____ (Firm Name)

_____ (Print or Type Your Name)

_____ (Date)

Please complete this form and return to:
Arizona Foundation for Legal Services & Education - IOLTA
4201 N. 24th Street, Suite 210, Phoenix, AZ 85016-6289
E-mail: aziolta@azflse.org - Fax: 602-773-3105

APPENDIX C: Practical Suggestions from the State Bar Trust Account Examiners

- Do not act in haste when signing checks to be disbursed from or deposited to a trust account. For example, an employee had a lawyer endorse checks for deposit when the lawyer was in a hurry to get out of the office. The lawyer failed to note that the office deposit stamp was not put on the back of the check. The checks were deposited into the employee's personal accounts. This activity did not come to the attention of the lawyer until clients complained about their bills.

- Use pre-numbered checks and periodically examine the sequential order of blank, void and canceled checks. Question any unexplained break in numbers. Voided checks should be retained. Keep blank checks under a responsible person's control during the day and secured at night. In addition, ensure that all checks are accounted for when an employee resigns or is terminated.

- Legal fees paid in cash are difficult to control. Office policy should require that a receipt must be given to any client who pays in cash, and the lawyer should regularly ask clients who pay in cash if they receive a receipt. The numbers for receipts in the receipt book should also be examined periodically to determine if any receipts were removed or voided.

- The tasks of posting, depositing and disbursing trust account funds should be handled by different members of the staff. If this is not possible, a lawyer may want to reconcile the trust account periodically or have an independent party do so.

- Resolve discrepancies in a trust account reconciliation as soon as possible.

- Try not to sign blank checks, and do not make a check out to cash or bearer.

- A client's file should contain documents supporting disbursements.

- Ensure deposits are made in a timely manner, daily if possible.

- Bank statements and correspondence regarding the trust account should be opened and reviewed by someone other than the bookkeeper.

- Require supporting documentation (e.g. bank statements, canceled checks, deposit slips, correspondence, etc.) of accounting reports and reconciliations.

- Personally investigate questionable activities pertaining to the trust account (e.g. lack of fee payments, missing correspondence, etc.)

- Question life style changes (e.g. increased social activities or travel, new wardrobe, new car, etc.) of individuals with access to the trust account.

- Examine signature(s) on trust account checks for forgery.

- Compare the number of canceled checks received from the bank to the number returned as indicated on the monthly bank statement.

- Question any change or attempted change of a payee's name on a check.

- Personal, professional, or financial problems (e.g., family illness, marital problems, drinking, bankruptcy, etc.) may be cause for embezzlement.

- Sloppy bookkeeping may be used to conceal embezzlement. If the responsible individual procrastinates in correcting the condition, and independent party should reconcile the account(s).

- Reconcile the trust account promptly after receiving a bank statement.

- Make sure that deposit slips agree with deposits posted on client's ledger, particularly when cash is involved.

- Confirm that the amount on the check coincides with the check stub or other supporting documentation.

- Embezzlement occurs more frequently when an unsupervised person has total responsibility for the trust, office, and/or payroll accounts.

- Embezzlers tend to make draws on the office operating account first and later make draws on the trust account.

- Question a negative attitude or poor work performance of an employee maintaining the trust account especially if the employee was passed over for a promotion.

- Beware of an employee who is overly possessive of the trust account.

- The absence of minimum internal controls and sound accounting practices creates a situation in which there is a strong potential for embezzlement to go unnoticed.