Third Edition: 2023

CLIENT TRUST ACCOUNT BASICS

A Handbook for Kentucky Lawyers

Lawyers Mutual of Kentucky

KENTUCKY IOLTA FUND
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Client Trust Account Basics: A Handbook for Kentucky Lawyers **(Third Edition) provides general information only and is not legal advice.**

This handbook should answer many basic questions about client trust accounts, but it is not a substitute for legal advice or for independent legal research on specific situations.

When faced with a specific situation or dilemma, Kentucky lawyers are urged to utilize the Kentucky Bar Association Ethics Hotline (SCR 3.530). The Ethics Hotline is an invaluable service to the Bar that can help avoid a misstep in managing the property of others.

Please note, this is **not a publication of the Kentucky Bar Association** and is not binding on those officials responsible for bar discipline.

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INTRODUCTION

This revamped Third Edition[1] of *Client Trust Account Basics* continues the joint effort of the Kentucky IOLTA Fund and Lawyers Mutual Insurance Company of Kentucky (Lawyers Mutual) to provide Kentucky lawyers with information about their fiduciary obligation to clients when managing client trust accounts.

Client trust account management is a unique aspect of a lawyer's professional responsibility. It involves specific fiduciary duties that are primarily administrative in nature. A lawyer out of trust — the books do not balance or some other fiduciary duty is breached — has violated the Kentucky Rules of Professional Conduct and is subject to discipline. Violations can lead to bar discipline, up to and including disbarment. Lawyers should be proactive, taking the time to understand the duties owed and to implement policies and procedures that ensure fulfillment of those duties.

HOW TO USE THIS HANDBOOK

This Handbook is aimed at aiding Kentucky lawyers in the day-to-day ethical management of client trust accounts.

For lawyers new to client trust account management, reading the full Handbook is the best way to form a solid understanding of the duties and responsibilities owed to clients. Keep in mind that even if a lawyer is entering a firm that has staff handling the firm's finances, the lawyer still must understand their duties and responsibilities owed to the client.

Thereafter, this Handbook is designed to serve as a reference guide. Use the interactive table of contents to jump to specific sections and find pertinent answers. Additionally, as you read you will notice links to related content internally as well as links to external resources for additional information and research. Utilize these resources to build upon the basics covered here, and reach out to **Lawyers Mutual** or the **IOLTA Fund** if you have additional questions about the content.

While this Handbook should answer many basic questions about trust accounts, it is not legal advice. Additionally, while comprehensive, the Handbook is focused on the basics of client trust account management and not intended to be all-inclusive. Specific situations require research beyond what is available here. Contacting the Kentucky Bar Association (KBA) Ethics Hotline is urged in questionable situations (SCR 3.530). The Ethics Hotline is an invaluable service to the Bar that can help avoid a misstep in managing the property of others.

1 Prior editions were titled *Client Trust Account, Principles & Management for Kentucky Lawyers.*

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CHAPTER 1

CLIENT TRUST ACCOUNTS: WHAT ARE THEY?

The Kentucky Rules of Professional Conduct require lawyers to "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." (SCR 3.130 (1.5)(a)). Often, lawyers have possession of client money, including retainers and settlement funds, which must be placed into a client trust account.

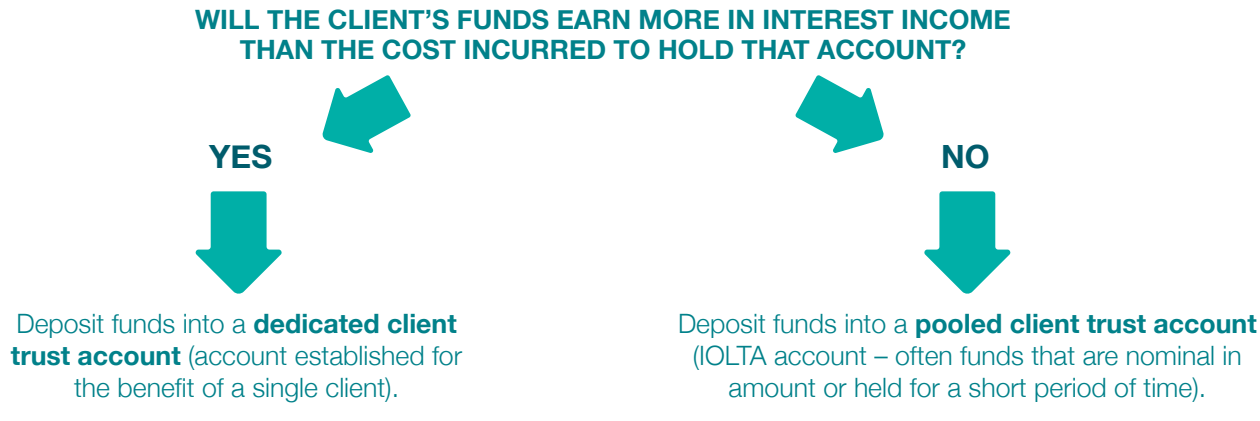
There are two general types of client trust accounts, which are often confused or discussed interchangeably. Before we jump into the rules, let's define these important and distinct terms:

1. **Dedicated Client Trust Account:**
   An account holding client funds for a single client.
2. **Pooled Client Trust Account:**
   An account holding client funds for multiple clients.

Keep in mind, client trust accounts ***must*** be interest bearing. Additionally, the lawyer may not collect the interest from either type of account. Where the interest goes is discussed below.

SO WHICH CLIENT TRUST ACCOUNT SHOULD YOU USE?

The lawyer must decide which type of client trust account is most appropriate: either the dedicated client trust account or the pooled client trust account. Consider the following flow chart based on SCR 3.830 when determining which is the right account:



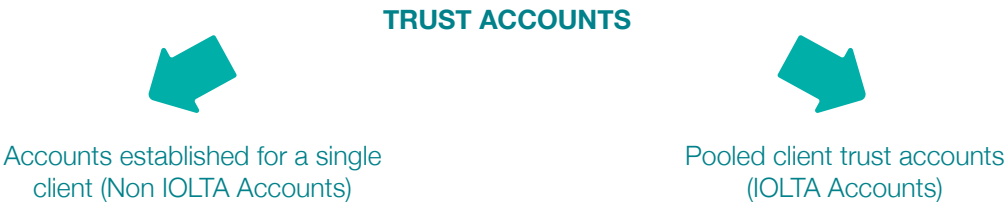
How do you determine whether the client funds could earn interest income greater than the costs incurred? The rule specifically guides lawyers to ask two questions:

- Are the client funds nominal?
- Will the client funds be held for a short period of time?

Examples of the funds described in SCR 3.830 that should be deposited into an Interest on Lawyers' Trust Account (IOLTA) account often include retainer payments or settlement amounts that will soon be distributed among several parties including the client, the attorney as a fee, and any claims required to be paid by law or paid by agreement with the client.

If you determine a dedicated client trust account is required, the IOLTA rule does not apply. The interest earned is client property and must be paid to the client.

If you determine a pooled client trust account is needed, the IOLTA rule does apply. Interest earned on the account is paid to the IOLTA Fund to provide grants for legal aid, local bar pro bono programs, and projects to improve the administration of justice. IOLTA is discussed in more detail in Chapter 2.



THE RULES

There are several rules governing the safekeeping of client trust funds. Rule 1.15 applies to **all** trust accounts (and any client property in the lawyer's possession). Rule 3.830 applies only to IOLTA accounts (i.e., pooled client trust accounts). Lawyers – especially those new to private practice – should read both rules in full.[2] However, we have included a summary, below, to help lawyers refresh their knowledge and have context on the two rules' main requirements.

SCR 3.130 (1.15), Safekeeping Property

- Lawyers must hold client property in their possession separate from their own (*although a lawyer is permitted to deposit their own money as necessary to pay bank service charges*). *1.15(a) & (d)*
- Lawyers should hold that property with the care required of a professional fiduciary. 1.15, Comment 1
- Client trust accounts must be maintained in a bank:
  - · in the state where the lawyer's office is situated (or elsewhere with client's consent); and,
  - · that has agreed to notify the Kentucky Bar Association of any overdrafts on the account. 1.15(a)

2 These rules are included in **Appendix A** for reference. These rules are subject to updates by the Kentucky legislature and Kentucky Supreme Court. For an exhaustive list of rules in their most updated versions, please visit the **Kentucky Court of Justice page**.

- Lawyers must promptly provide clients:
  - · notification when receiving funds in which the client has an interest;
  - · delivery of funds or property the client is entitled to receive; and,
  - · a full accounting of the client's property upon request. 1.15 (b)
- Advance retainers (legal fees and expenses paid in advance) must be deposited into a client trust account. Withdrawals are to occur only when fees are earned or expenses are incurred. 1.15(e). See Rule 1.5(f) for more information about the exception for properly designated advanced fees.

SCR 3.830 Kentucky IOLTA Fund

- Client funds that will not earn interest income in excess of the cost incurred to secure that income (e.g., bank service charges) must be held in an interest-bearing, pooled client trust account (IOLTA account).
- IOLTA accounts must be held at a participating financial institution. 3.830(3)
- Attorneys must complete a **New Account Enrollment Form** each time they open a new IOLTA account.
- By September 1 of each year, attorneys must certify their compliance with or exemption from the IOLTA program. This certification should be completed on the attorney's **KBA member profile** and is conveniently incorporated into the KBA's annual dues payment process. 3.830(13)
  - · Common exemptions include not being engaged in the private practice of law and not practicing in Kentucky. 3.830(14)
- Interest collected by the Kentucky IOLTA Fund is used to make annual grants to legal services and *pro bono* programs and to other law-related programs for the benefit of the public.

Additional Rules to Keep in Mind

Several other rules of professional conduct have implications for proper client trust account management. These include the following:

1. **Rule 3.130 (1.5)**, Fees
2. **Rule 3.130 (1.8)**, Conflict of Interest
   (a) concerning business transactions with clients
   (e) concerning financial assistance to clients
3. **Rule 3.130 (1.16)**, Declining or Terminating Representation
4. **Rule 3.130 (5.1)**, Responsibilities of Partners, Managers and Supervisory Lawyers
5. **Rule 3.130 (5.2)**, Responsibilities of a Subordinate Lawyer
6. **Rule 3.130 (5.3)**, Responsibilities Regarding Nonlawyer Assistants
7. **Rule 3.130 (8.4)**, Misconduct
8. **Rule 3.820**, Clients' Security Fund

CHAPTER 2

INTEREST ON LAWYERS' TRUST ACCOUNTS FUND (IOLTA)

The Kentucky Interest on Lawyers' Trust Accounts (IOLTA) Fund is a fund of The Kentucky Bar Foundation, Inc. and exists to assist or help establish legal services programs, *pro bono* programs, and other law-related programs for the public's benefit.

WHAT IS IOLTA?

IOLTA stands for Interest on Lawyers' Trust Accounts. IOLTA is a unique and innovative way to increase access to justice for individuals and families living in poverty and to improve our justice system. Without taxing the public–and at no cost to lawyers or their clients–interest from certain lawyer trust accounts is pooled to provide civil legal aid and support improvements to the justice system. IOLTA programs exist in all 50 states, Puerto Rico, and all Canadian provinces and have for many years.

What is IOLTA?

INTEREST
ON
LAWYERS'
TRUST
ACCOUNTS

ARE ALL TRUST ACCOUNTS IOLTA ACCOUNTS?

NO. Holding client funds in trust is a requirement under the Rules of Professional Conduct. There are two types of trust accounts: dedicated and pooled client trust accounts.

- **Dedicated client trust accounts** are established for the benefit of one client. These are not subject to IOLTA and are sometimes referred to as non-IOLTA accounts.
- **Pooled client trust accounts** are established to maintain the funds of multiple clients. These are subject to IOLTA and are therefore commonly referred to as IOLTA accounts.

In both cases, the account must be interest-bearing. In neither case may the attorney collect interest earned on that account. For more information about the different client trust accounts, please see Chapter 1.

HOW DOES IOLTA WORK IN KENTUCKY?

The Kentucky IOLTA Fund was established in 1986 by Kentucky Supreme Court Rule 3.830, and participation in the program became mandatory for Kentucky attorneys on January 1, 2010. The program uses the advantage of pooling client trust funds to generate interest in excess of service fees and administrative costs. Attorneys in the program deposit small or short-term trust funds into pooled client (interest-bearing) accounts, and the interest earned on those funds is paid directly to the IOLTA Fund. Client funds remain under the control of the attorney, who continues to maintain his or her trust account, and neither the attorney nor the client is taxed on interest generated from the account. The interest collected is awarded annually by the Kentucky IOLTA Fund, with approval by the Kentucky Supreme Court, in the form of grants.

WHO BENEFITS FROM IOLTA?

The Kentucky IOLTA Fund has awarded nearly $20 million in grants since 1988. The interest received by the IOLTA Fund is disbursed in the form of grants for legal aid, local pro bono programs, and other projects that improve the administration of justice in Kentucky. Grant recommendations are prepared by the IOLTA Board of Trustees annually and submitted to the Kentucky Supreme Court for review and approval. While the makeup of grants varies from year to year, and there is no established percentage of funds for any specific program, a significant portion of the funds has supported Kentucky's four regional civil legal aid programs. Additionally, grants have been made annually to the three Kentucky law schools for fellowships that allow law students to intern with law-related public service organizations at no cost to the organization.

WHO IS REQUIRED TO PARTICIPATE IN THE IOLTA PROGRAM?

Pursuant to Kentucky Supreme Court Rule 3.830, all Kentucky attorneys must participate in the IOLTA program unless they qualify for an exemption. However, unless there is a need for a pooled client trust account, attorneys need not establish an IOLTA account in order to comply with the Rule.

WHO IS EXEMPT FROM PARTICIPATING IN THE IOLTA PROGRAM?

A lawyer is exempt from participating in the IOLTA program if he or she falls within one of the specific exemptions in **SCR 3.830(14)**. The more common exemptions include attorneys who are not engaged in private practice, who do not have trust accounts in Kentucky, or who do not manage or handle client trust funds.

WHEN AND HOW DO I CERTIFY MY COMPLIANCE WITH SCR 3.830?

SCR 3.830(13) requires that all Kentucky lawyers certify annually, on or before September 1 of each year, that they are in compliance with, *or exempt from*, the provisions of the rule requiring participation in IOLTA. Attorneys certify their compliance by updating their IOLTA information on their **Member Profile Page** when paying KBA dues each year through their Kentucky Bar Association online account.

WHICH KENTUCKY BANKS PARTICIPATE IN THE IOLTA PROGRAM?

Currently, 130 banks across Kentucky offer IOLTA accounts to their customers. Many have recognized the important public purpose served by the IOLTA program and have waived fees on these accounts, in addition to paying favorable interest rates. The support and generosity of these partner banks enables the IOLTA Fund to award significant grants for legal aid each year. If your bank does not presently participate in the IOLTA program and is interested in becoming a participant, please have your bank contact the Kentucky IOLTA Fund. Should a lawyer's bank refuse to offer an IOLTA account, the attorney will need to move his or her trust account to a bank that does offer IOLTA accounts. The IOLTA Fund can help you to locate a participating bank in your area.

HOW DO I OPEN AN IOLTA ACCOUNT?

To open an account, an attorney first opens a standard, non-interest-bearing client trust account. Next, the attorney is required to complete a **New Account Enrollment Form** any time a new account is established. This form simply serves as the attorney's authorization for the Kentucky IOLTA Fund to earn any interest from the account. Once that online form is submitted, the Kentucky IOLTA Fund will communicate via secure email to IOLTA's contact at the participating bank. The bank will then convert the account to interest-bearing IOLTA status. No further action is needed and there should be no delay in the attorney's use of the account.

The only thing that changes when an attorney's client trust account is "converted" to IOLTA is that it becomes interest-bearing and any interest from the account is forwarded to the Kentucky IOLTA Fund direct from the bank. Nothing else changes about the day-to-day operation of the account. There is a common misconception from attorneys and banks alike that the Kentucky IOLTA Fund is approving the account; however, this is not the case.

WHO PAYS THE BANK SERVICE FEES ON AN IOLTA ACCOUNT?

Enrolling a client trust account in the IOLTA program does not result in additional bank service charges for lawyers because the IOLTA Fund pays any reasonable bank charges or service fees associated with the account's interest-bearing status. Lawyers remain responsible for all other fees, such as check printing charges, wire transfer fees, and overdraft fees.

WHO DO I CONTACT IF THERE IS AN OVERDRAFT IN MY IOLTA ACCOUNT?

Overdrafts are managed by the Kentucky Bar Association Office of Bar Counsel (OBC). If your IOLTA account is overdrawn, contact the OBC at (502) 564-3795. Overdrafts are **not** managed by the Kentucky IOLTA Fund office.

WHAT SHOULD I DO WITH UNCLAIMED FUNDS IN MY IOLTA ACCOUNT?

SCR 3.830(21) allows unclaimed funds to be remitted to the Kentucky IOLTA Fund provided that reasonable efforts, as set forth in the rule, to locate the rightful owner of the funds have been conducted. Remit unclaimed funds by completing an **Unclaimed Funds Remittance Report Form**, which is available on the Kentucky IOLTA Fund website. The form can be mailed, along with a check for the funds, to the Kentucky IOLTA Fund.

KENTUCKY IOLTA FUND AND CLASS ACTION RESIDUAL FUNDS.

Kentucky Rule of Civil Procedure (CR) 23.05 sets forth the procedures governing a proposed settlement, voluntary dismissal, or compromise of a class action. CR 23.05(6) addresses the disposition of any "residual funds," which are funds remaining after the payment of all approved claims, expenses, costs, fees, and other court-approved disbursements to implement the relief granted. In actions where the claims process has been exhausted and residual funds remain, 23.05(6)(b) requires that not less than 25% of the residual funds be disbursed to the Civil Rule 23 Account maintained by the Kentucky IOLTA Fund. Such funds are then allocated to Kentucky's civil legal aid organizations to support activities and programs that promote access to the civil justice system for low-income residents of Kentucky.

For further information regarding the Kentucky IOLTA Fund,
email Executive Director Guion L. Johnstone at gjohnstone@kybar.org or
Program Manager Gwen Smallenburg at gsmallenburg@kybar.org
or call (502) 564-3795.

CHAPTER 3

AN OVERVIEW OF DUTIES OWED TO CLIENTS WITH REGARD TO CLIENT PROPERTY

Comment 1 to SCR 3.130 (1.15), Safekeeping property: A lawyer should hold property of others with the care required of a professional fiduciary.

WHAT IT MEANS TO BE A FIDUCIARY

A lawyer's relationship with a client is that of a fiduciary. This means that clients place a special trust and reliance in lawyers to act for the clients' benefit instead of their own. Lawyers must act in good faith and with candor in all dealings with clients.

This fiduciary duty is reflected in the overarching professional responsibility rules concerning client confidentiality and conflicts of interest. Rule 1.15 codifies many of the common law requirements of a fiduciary (i.e., an agent's accountability for a principal's property) and gives the KBA the authority to discipline a lawyer for failing to properly account for client and third-party property.

THE FIDUCIARY DUTY OVERVIEW

Rule 1.15 addresses the safekeeping of all client and third-party property in the lawyer's possession. The following overview is focused on the basics of the lawyer's fiduciary duty in handling client funds as it relates to client trust accounts. Section IV, below, will then provide more details on the application of these principles.

For information about fiduciary duties specifically related to non-monetary property and the property of third-parties, visit the Practice Management section of Lawyers Mutual's website or contact Courtney Risk at risk@lmick.com for additional resources.

You can delegate authority, but you can't delegate responsibility!

A lawyer is responsible for all funds and property received by the firm in connection with their representation of a client. The internal management of funds and property may be delegated. Often, a managing partner will be tasked with the day-to-day management of the trust account with the assistance of non-lawyer office staff. This delegation is common and appropriate–as long as policies are in place to ensure compliance with ethical duties. See Rules 5.1-5.3.

If things go wrong, the lawyer handling the matter as well as the managing partner(s) are all ultimately responsible for a breach of fiduciary duties, including mismanagement of client trust accounts. Partners and managing lawyers have a responsibility to ensure proper procedures are adopted and followed to ensure the ethical behavior of all employees in the firm. Rule 5.1. Additionally, all supervising lawyers–whether supervising another lawyer or a non-lawyer employee–have a duty to ensure ethical obligations are met. Rule 5.3.

To meet this non-delegable responsibility lawyers must first develop good procedures to prevent common errors, like mixing client and lawyer funds and improper documentation of transactions. Adoption of financial management systems that require input of necessary information (source of deposits, reasons for withdrawals, etc.) can often prevent many of the most common record keeping errors. These systems can also provide regular reports that can assist with the required oversight of the client trust accounts.

Lawyers must also carefully supervise and train those in the firm tasked with the day-to-day management of client trust accounts to ensure compliance with the adopted procedures. Effective supervision includes:

- Regular discussion of assigned tasks
- Monthly review of client trust account transactions and reports
- Annual training on office procedures
- Use of outside auditors

PRACTICE TIP Do not allow nonlawyer signatories on trust accounts.

Additional information about effective supervision is available on Lawyers Mutual's website.

Keep client funds separate!

The first step in safekeeping client funds is to meet the requirement of segregating said funds from firm monies and a lawyer's personal funds. This means depositing client funds in a client trust account separate from firm operating accounts and lawyer personal accounts. Practical difficulties such as a quick turnaround for disbursement do not excuse failure to deposit funds in a client trust account. Nor can the requirement be avoided by a lawyer personally holding the funds until dispersal. The value of this strict requirement for lawyers is that it creates an audit trail that affirmatively shows exactly how funds were disbursed.

PRACTICE TIP Commingling happens when client funds are deposited into the operating account AND when earned fees are left in the trust account. Neither is permissible.

Fees must be earned before withdrawing!

One common use of the client trust account is to deposit advance retainers paid in anticipation of fees and expenses to be incurred. However, a lawyer must first earn the fee before withdrawing the funds from the client trust account and transferring them to the firm's operating account. The client may also be responsible for paying expenses per your fee agreement, but those must be incurred before withdrawing from the client trust account.

PRACTICE TIP **Use your fee agreement to spell out how and when the fee is earned.**

Promptly notify clients of the receipt of funds.

Rule 1.15(b) requires the lawyer to promptly notify clients when receiving funds in which the client has an interest. While prompt is subject to interpretation, lawyers who delay notification for a matter of months may receive discipline for failure to promptly notify. Even if the client has given the lawyer instructions on how received property is to be managed, the lawyer must still provide prompt notice of receipt.

The best practice is to notify the client, in writing, as close in time to receipt of the property as reasonably can be made.

Be equally prompt in delivering funds to clients.

Rule 1.15(b) also requires the lawyer to promptly deliver funds to the client once the client is entitled to receive said funds. The most common scenarios are the disbursement of the client's portion of settlement funds or the reimbursement of unearned fees. Prompt is, again, subject to interpretation. Lawyers have been disciplined for delays in disbursements of five weeks, several months, and–in extreme cases–for years.

The best practice is to not disburse funds received until:

- funds received are unconditionally credited to the client trust account by the bank; and,
- all necessary documents are executed and, if applicable, filed appropriately.

PRACTICE TIP **"Available" does not mean "collected." If the funds have not been collected, they are not there and should not be disbursed.**

Once these steps are completed, the lawyer should disburse as promptly as good business practice will permit. In the event the funds are in dispute, the funds should remain in the client trust account until the dispute is resolved. The fact of the dispute and the efforts toward resolution should be well documented.

Additional information about prompt disbursements is discussed in Chapter 4, Section 2, and management of disputed funds is discussed in Chapter 4, Section 4.

Keep complete records!

Compliance with Rule 1.15 requires a detailed accounting of how funds and property were managed from receipt to disbursement. Firm procedures must require detailed records for every transaction. This allows the lawyer to easily comply with Rule 1.15(b)'s requirement to promptly render a full accounting to the client upon request. The basics of client trust account recordkeeping are covered in Chapter 6 and Appendix C.

Be sure to terminate representation according to Rule 1.16

A representation typically has a clear ending: the lawyer has handled the matter to conclusion and disbursed all funds with appropriate accounting followed by a **written termination letter**. However, what happens if the client and lawyer must part ways before the matter concludes? In those situations when the lawyer withdraws or is discharged by the client, fiduciary duties continue until the representation is properly terminated. Rule 1.16(d) requires the lawyer to "take steps to the extent reasonably practicable to protect a client's interests." A lawyer in this situation is required to surrender papers and property to which the client is entitled and refund any advance payment of fees that have not been earned. Keep in mind, lawyers may request payment for the cost of copying the file, but they cannot condition the return of the file on receiving that payment.

Retain client trust account records for five years after termination.

Once the representation is terminated, Rule 1.15 requires the lawyer to maintain client trust account records for five (5) years. A more complete file retention overview is included in Chapter 7, Section 3.

BREACH OF FIDUCIARY DUTY: MISAPPROPRIATION

The most serious client trust accounts breaches are usually organized under the heading of misappropriation. In this context, misappropriation is a term of art indicating:

> **Conversion:** Examples of conversion include: stealing; unauthorized temporary use of client funds regardless of purpose; check kiting; misapplying funds earmarked for a special purpose; failure to return unearned fees or unused client funds; improperly withholding fees from client funds; and using one client's funds to pay another's charges.
>
> **Commingling:** Commingling occurs when a lawyer fails to segregate client funds from the firm's funds or the lawyer's personal funds. This results in the client funds losing their separate identity. The rule also precludes depositing the lawyer's own funds in the account, even if there are no client funds in the trust account.

In either situation, the fact that no funds are misapplied or are lost by a client is not a defense against misappropriation. Lawyers that misappropriate funds could face bar discipline as well as civil or criminal consequences.

Lawyers have strict liability for any irregularity in a client trust account, even when no client suffers a loss. Even when the irregularities result from minor bookkeeping errors that are quickly corrected and no harm is

done—it is a per se offense that needs to be addressed. Contacting the ethics hotline for an opinion on what next steps you should take and whether the client needs to be notified is recommended.

MITIGATING BREACH OF FIDUCIARY DUTY

When any irregularity in a client trust account occurs, lawyers should utilize the ethics hotline for guidance on next steps. Additionally, lawyers may also want to reach out to their legal professional liability carrier for assistance in mitigating any additional risk or losses. Poor supervision of nonlawyer staff, sloppy records, and dishonored client trust account checks are just a few of the causes of misappropriation that can also lead to bar discipline. Even if a minor mistake does not result in discipline, a pattern of minor mistakes can result in serious sanctions. Any significant problem with a client trust account carries a longer-term risk of suspension or disbarment.

If your carrier offers mitigation on errors before they become complaints or lawsuits, you will want to tap into their expertise to navigate any necessary changes to your administrative practices. Lawyers Mutual of Kentucky encourages its insureds to report possible errors as soon as possible so the claims team can get to work quickly to minimize or potentially avoid further losses. Other carriers vary on their claims mitigation policy; you should inquire about their specific services and requirements.

CLIENT SECURITY FUND

What does it cover? A client's pecuniary loss due to their lawyer's fraud or dishonest acts.

What does it *not* cover? Client losses related to a lawyer's negligence.

The Client Security Fund (SCR 3.820) is a great safety net for clients who suffer certain losses at the hands of their lawyer. The Fund, however, is not a substitute for legal professional liability coverage. Lawyers should still obtain malpractice insurance for coverage of negligent acts.

CHAPTER 4

HOW TO PROPERLY HANDLE YOUR CLIENT TRUST ACCOUNT

The rules and considerations in this section apply to all client trust accounts regardless of whether it is a dedicated client trust account (non-IOLTA account) or a pooled client trust account (IOLTA account). Practitioners should refer to this guide any time they are responsible for client funds and/or other client property.

PROPER DISBURSEMENT

The rule requires **prompt** disbursement of funds to clients. The best practice is to wait until all funds received by a lawyer for disbursement have been collected by the bank from the other financial institution and there is no longer a risk of the funds being pulled back out of the account. “Available Balance” does not mean “collected.” Lawyers should understand all aspects of how deposited funds are managed, put on hold, dishonored, and unconditionally credited to an account, including any applicable credit card deposit procedures. If you need help, ask the bank’s personnel for guidance.

Once the funds are collected and all required documents executed, then the lawyer should disburse as promptly as good business practice will permit. Explain this procedure to clients at the inception of the engagement and include it in letters of engagement so clients do not have unreasonable expectations about when they will receive funds.

CASH TRANSACTIONS

If you receive cash payments from clients, be aware of IRS reporting requirements. This resource from the IRS provides an overview to help you determine whether you need to file Form 8300.

PROMPT DISBURSEMENT

The rule requires **prompt** disbursement of funds to clients. The best practice is to wait until all funds received by a lawyer for disbursement have been collected by the bank from the other financial institution and there is no longer a risk of the funds being pulled back out of the account. "Available Balance" does not mean "collected." Lawyers should understand all aspects of how deposited funds are managed, put on hold, dishonored, and unconditionally credited to an account, including any applicable credit card deposit procedures. If you need help, ask the bank's personnel for guidance.

CAUTION Lawyers are often the target of financial transaction scams, especially those involving wire transfers. See the section, Client Trust Account Scams, in Chapter 7 for more information about what to look for to prevent fraud or theft by a third-party.

Once the funds are collected and all required documents executed, then the lawyer should disburse as promptly as good business practice will permit. Explain this procedure to clients at the inception of the engagement and include it in letters of engagement so clients do not have unreasonable expectations about when they will receive funds.

PRACTICE TIP Do not disburse funds to clients and ask that they hold the check for a period of time.

CLIENT INSTRUCTIONS FOR DISBURSEMENT

A lawyer may not make a disbursement unless it is either authorized by the client or it is authorized by contract, statutory lien, court order, or other law. This means the client's authorization is needed to pay a lawyer's fee or incurred expenses as well as most third-parties that might have an interest in the client's funds. The best practice is to get advance approval for how and when funds will be disbursed at the inception of the representation in a letter of engagement signed by the client. If, during the course of the representation, the lawyer learns of additional creditors or other third-parties that have an interest in the client's funds, the lawyer should obtain updated written instructions for any disbursement approved by the client.

Lawyers should consider the following practical scenarios when developing their own policies and procedures:

- Obtain written client authority before hiring experts and other high expense aspects of case preparation (i.e., don't surprise the client with a huge disbursement).
- Get written client authority to pay creditors with any interest in the recovery. This is particularly important for those individuals the lawyer has personally engaged, such as medical services required to develop a personal injury case. If the client gets all of the recovery proceeds and fails to pay creditors, the lawyer could be liable. Almost as bad, it is the lawyer's credibility that suffers in the next case when seeking needed services.
- When disbursements are made to satisfy a contract obligation, statutory lien, court order, or other law, provide clients with the documents requiring disbursement.

- Consider having the client pay large expenses directly while the case is ongoing and prior to final recovery disbursement. This simplifies things at the conclusion of the matter for all concerned.
- Confirm in writing with a creditor or third-party claimant the exact amount due before advising a client to approve a disbursement.

Remember to never disburse funds to a creditor or other third-party before checks providing funds for the disbursement are available in the client trust account, as discussed under the Prompt Disbursements section, above.

DISPUTED DISBURSEMENTS

Rule 1.15(c) provides limited guidance on how to proceed if the lawyer and client are not in agreement about their respective interests in the funds held in the client trust account. Although 2009 rule amendments had added procedures for handling disputed funds, these were removed in 2014. The rule now states the lawyer shall keep the funds separate until the dispute is resolved. Further, "[t]he lawyer shall promptly distribute all portions of the funds or other property in which the interests are not in conflict."

When a dispute arises, call the KBA Ethics Hotline for guidance. Also, before pursuing fees owed, it may be prudent to contact your professional liability carrier. One of the leading triggers for a malpractice claim is the lawyer filing suit over a fee dispute. You will want to explore all of your options with counsel before taking action to collect fees owed.

CHAPTER 5

BANKING CONSIDERATIONS

INSURING CLIENT TRUST ACCOUNTS

Rule 1.15 does not require that client trust accounts, in general, be insured by the FDIC. However, Rule 3.830 requires pooled trust accounts (IOLTA accounts) to be established with a participating financial institution:

- authorized by federal or state law to do business in Kentucky, and
- insured by the Federal Deposit Insurance Corporation or its equivalent.

Even if a lawyer is exempt from participating in the IOLTA program, it is a good risk management practice nonetheless to deposit all client funds in financial institutions that are insured, either by the FDIC or its equivalent. Lawyers should also ensure account balances are maintained in accordance with the coverage requirements.

For details on FDIC coverage for fiduciary accounts, check out the following resources:

- "**Your Insured Deposits — FDIC's Guide to Deposit Insurance Coverage**"
- **Fiduciary Accounts**
- **When a Bank Fails – Facts for Depositors, Creditors, and Borrowers**

Lawyers can also visit **www.FDIC.com** and search fiduciary accounts for the most up-to-date resources.

CREDIT CARD DEPOSITS

Payment by credit card for legal services performed by law firms was approved in **KBA E-172 (1977)**. This opinion is one of first impression concerning the basic question of whether credit card payments may be accepted at all by law firms in Kentucky. It did not consider many ethical issues concerning credit card fee collection. Specifically, it addressed only payment of earned fees but not retainers. In 2007, **KBA E-426** filled the gap by providing both the professional responsibility guidance and the client trust account management considerations required to confidently accept credit card payments for unearned fees and advanced costs, and to guard against commingling funds.

For a more detailed look at the overlap between credit cards and trust accounts, see **Lawyers Mutual's article on the issue**.

BANK INTEREST

All client trust accounts must be interest-bearing. Lawyers are prohibited from earning the interest paid on client trust account funds. Lawyers are also prohibited from using earned interest to pay for bank charges on the account; charges are discussed in more detail, below.

Interest earned on dedicated client trust accounts (non-IOLTA) must be paid to the client upon disbursement. Interest earned on pooled client trust accounts (IOLTA) are paid directly to the IOLTA fund by the financial institution. The IOLTA Fund then uses the funds to provide grants to law-related public interest projects. The IOLTA program is discussed more fully in **Chapter 2**.

BANK SERVICE CHARGES

Clients may be charged for specific bank service charges directly attributable to a particular client–for example, a wire transfer fee. However, clients may not be charged for bank service charges that are not directly attributable to the specific client. For example, general administrative expenses which include checks or monthly fees on pooled client trust accounts.

Rule 1.15(d) permits lawyers to deposit firm funds in client trust accounts for the sole purpose of paying bank service charges, avoiding misappropriation of client funds. Lawyers must keep accurate records of which portion of the account funds are the firm's. It is feasible with some banks to link firm operating accounts to client trust accounts for automatic replenishment of funds necessary to cover bank charges. This procedure avoids even brief improper use of client funds to cover bank service charges.

CHECK SIGNATURE AUTHORITY

The recommended practice is for a lawyer to sign all checks. Delegation of this authority is discouraged by risk managers as well as the ABA's Model Rule on Financial Recordkeeping, which is cited in Kentucky's Rule 1.15, Comment (1). The Model Rule states that "[w]ith respect to trust accounts required by [Rule 1.15 of the Model Rules of Professional Conduct]: (1) only a lawyer admitted to practice law in this jurisdiction shall be an authorized signatory on the account…."

Best practices for check signatures include:

- Signers should be limited to the managing partner or lawyer(s) who possesses managerial authority in a firm.
- Never use signature stamps or computer-generated signatures.
- Also, never obtain a debit card for the client trust account. Similarly, never use ATMs to withdraw or deposit client funds. This is because unauthorized persons may gain access to the card and an adequate paper record is not generated by ATM receipts.

OVERDRAWS AND OVERDRAFTS

An overdraw occurs when funds of one client are erroneously expended for the benefit of another client from a pooled client trust account. An overdraft occurs when a check is dishonored for lack of sufficient funds in the account. In either circumstance the lawyer is out of trust and in violation of Rule 1.15. Immediately upon discovering the problem the lawyer must take corrective action by depositing funds in the client trust account

to bring it back into balance. The cause of the overdraw or overdraft should be determined, corrected, and documented. A call to the Ethics Hotline and/or your malpractice carrier may also be warranted if this occurs.

KBA OVERDRAFT NOTIFICATION REQUIREMENT

Rule 1.15 (a) requires that client trust accounts be maintained in a bank that has agreed to notify the KBA of any overdraft. The KBA Office of Bar Counsel has defined an overdraft as:

> … an overdraft occurs whenever a properly payable instrument is presented against an account which contains insufficient funds to pay the instrument in full. It does not matter whether the instrument is actually dishonored or paid. When an overdraft occurs, it must be reported to the KBA. The bank does not need to concern itself with the circumstances of the overdraft or the reason it occurred, because the KBA will investigate to determine whether any further action is necessary.

Bank overdraft notices will trigger an inquiry by Bar Counsel, but an overdraft notice is not treated as a complaint until after the inquiry indicates this is appropriate, or if the attorney fails to cooperate with the inquiry.

PRACTICE TIP **The majority of overdraft notices received by Bar Counsel result from two scenarios – inadvertently writing a check out of the trust account rather than the operating account, and disbursing funds from the trust account that have not yet been collected into the account. Avoid these situations by ensuring the trust account checkbook is readily distinguishable from all others, and by refraining from disbursing any funds until the attorney is certain they are in the account.**

Note, lawyers should not enter into overdraft protection agreements with banks for client trust accounts. The ABA Model Rules for Trust Account Overdraft Notification, Rule 2, provides that "it would be improper for a lawyer to accept 'overdraft privileges' or any other arrangement for a personal loan on a lawyer trust account" "[i]n light of the purposes of this rule, and the ethical proscriptions concerning the preservation of client funds and commingling of client and lawyer funds." Even if a lawyer does enter into an overdraft protection agreement, this does not relieve the bank from notifying the KBA of an overdraft.

OUTSTANDING CHECKS

Client trust account checks not cashed for an appreciable period of time are a nuisance and can lead to errors in account management. This may also be an indication that the account includes unclaimed funds. There are various ways of coping with this problem to include printing on checks "Void after 90 days," contacting payees by telephone or certified mail if a large amount is involved, and placing a stop payment order on a check outstanding for too long. None of these approaches are guaranteed to solve the problem. It is important to coordinate with the bank to be clear on how bank procedures work and seek extra service in identifying voided outstanding checks.

CHAPTER 6

RECORDKEEPING

Rule 1.15, Comment 1: …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, e.g., ABA Model Financial Recordkeeping Rule.

Rule 1.15 requires a lawyer to preserve "complete records" of client trust accounts. In 1993, the ABA adopted the Model Rule on Financial Recordkeeping to provide clarity on what records must be maintained. Kentucky has adopted this model rule by specifically citing it in SCR 3.130 (1.15), Comment 1. It is important to note the ABA replaced this rule in 2010 with the Model Rule on Client Trust Accounts which is part of the larger, current Compendium of Client Protection Rules. When reviewing materials from the ABA and other sources, Kentucky lawyers must take care to refer to the correct version. Kentucky lawyers are only required to comply with the 1993 ABA Model Rule on Financial Recordkeeping; the 2010 rule is not binding on Kentucky lawyers.

This chapter summarizes the ABA Model Rule on Financial Recordkeeping. Lawyers should review the rule in Appendix B.

ACCOUNTING GLOSSARY

The Model Rule uses a few accounting terms to describe the types of records lawyers are required to maintain. While a variety of names are used for similar procedures, the Rule uses the following terms:

- Client Trust Account **Journal**: A record of all transactions in an account established for a single client, including:
  a. Record of deposits of funds, including date, source, description of each
  b. Record of disbursements, including date, payee, and purpose of each disbursement
- Client Trust Account **Ledger**: Records for all trust accounts documenting the following for each separate trust client (or beneficiary):
  a. Source of all funds deposited
  b. Owner of funds
  c. Amount of funds, at least monthly
  d. Description and amounts of deposits and withdrawals
  e. Names of persons receiving disbursements

The client trust account journal tracks all the transactions in an account–all deposits and withdrawals, including payment of bank fees. The client trust account ledger, on the other hand, focuses specifically on the client fund transactions. This ledger is particularly important for pooled client trust accounts to keep track of each client's current balance.

1. Reconciliation Reports: These records are to ensure that the ledgers, account journals, and bank statements all balance.

2. Checkbook Register: The register used to record checks as they are written on a client trust account comparable to the check stub book used for personal bank accounts.

Examples of the records, above, and practical application tips are available in **Appendix C**.

PRACTICE TIP **Reconciliation of a trust account is not just ensuring that the adjusted bank balance and checkbook register or general ledger match. Trust account reconciliation requires a three-way reconciliation, as the balance of all client ledgers and bank charges in the account must match the checkbook register and adjusted bank balance as well. While the Kentucky Bar Association Office of Bar Counsel is not permitted to give legal advice it does present the Trust Account Management Program, including a hands-on exercise culminating in a three-way reconciliation. For more information about the program, contact the OBC.**

RECORDKEEPING REQUIREMENTS

During the representation

The ABA Model Rule on Financial Recordkeeping states the records listed below must be maintained during the course of representation. Note, the Rule states records may be maintained electronically, so long as printed copies can be produced. Cloud-based accounting software is likely permissible under the rule which requires the records to be stored in a "readily accessible location." (paragraph (D)). Kentucky attorneys will want to review the Kentucky Formal Ethics Opinions on cyber security and cloud-storage, discussed in Chapter 7.

- Account Journals:
  - Record of deposits of funds, including date, source, description of each
  - Record of disbursements, including date, payee, and purpose of each disbursement
- Ledger records for all trust accounts documenting the following for each client, separately:
  - Source of funds
  - Owner of funds
  - Amount of funds, at least monthly
  - Description and amounts of deposits and withdraws
  - Names of persons receiving disbursements
- Client retainer and compensation agreements
- Copies of accountings to clients showing disbursements
- Copies of bills for legal fees and expenses

- Copies of records of disbursements made on behalf of clients
- Bank documents, including bank statements; checkbook registers or stubs; and records of deposits
  - Note: Due to the age of the model rule, some of the listed required documentation is not routinely provided or available (e.g., canceled checks). Lawyers should take steps to obtain and maintain any records routinely available from the bank and ensure that all transactions are documented fully
- Copies of both:
  - Monthly client balances
  - Quarterly reconciliations of the client's funds
- Any other document(s) needed for understanding a transaction

Additional recommended documents that lawyers should maintain to support client trust account transactions include:

- Client instructions or authorizations to disburse funds from the trust account
- All documents related to wire transfers in and out of the account
- Copies of all communications, including letters of engagement and termination

PRACTICE TIP **A written, signed fee agreement, even when not required under the rule, can go a long way in resolving fee disputes with clients, and the Bar Complaints that sometimes result.**

After termination of representation

Lawyers must maintain records related to client trust accounts for at least five years after the termination of a representation. When closing out a client file, the lawyer should ensure that records of all transactions for that client (and only that client) are included in the file. It is recommended that lawyers develop a file retention system that assures that required documentation is retained.

Firms must also prepare a plan for record maintenance in the event of the sale or dissolution of the firm. The ABA Model Rule on Financial Recordkeeping-which is incorporated into Kentucky's rules by reference-requires the partners or shareholders to make arrangements for maintenance of the records in the event the firm dissolves. Additionally, the Model Rule requires the lawyer selling a practice to make arrangements for the maintenance of the records. Additional information about succession planning is is discussed below in Chapter 7 under Succession and Planning.

CHAPTER 7

SPECIAL CONSIDERATIONS

CLIENT TRUST TECHNOLOGY CONSIDERATIONS

Lawyers frequently turn to vendors for software options designed for financial recordkeeping. Before choosing any software or IT vendor, lawyers should review two Kentucky ethics Opinions: **KBA E-437** (addressing use of cloud-computing) and **KBA E-446** (addressing cybersecurity).

Safeguarding Client Information in the Cloud (and Other Tech Vendors)

Ethics Opinion KBA E-437 states "lawyers must follow the Rules of Professional Conduct with regard to safeguarding client confidential information"—whether that information is in a "bricks-and-mortar law office, offsite warehouse, or online storage or service site in the cloud." See SCR 3.130(1.6), (1.9), (1.15), (1.18). The opinion concluded lawyers can use cloud storage for confidential client information, as long as the use complies with the following duties:

- Safeguarding client confidential information
- Acting competently in using cloud computing
- Properly supervising the provider of the cloud service
- Communicating with the client about cloud computing when such communication is necessary due to the nature of the representation

Based on these duties, the opinion provides a list of questions for lawyers to consider when reviewing potential cloud-based service providers.

- What protections does the provider have to prevent disclosure of confidential client information?
- Is the provider contractually obligated to protect the security and confidentiality of information stored with it?
- Does the service agreement state that the provider "owns" the data stored by the provider?
- What procedures, including notice procedures to the lawyer, does the provider use when responding to governmental or judicial attempts to obtain confidential client information?
- At the conclusion of the relationship between the lawyer or law firm and the provider, will the provider return all information to the lawyer or law firm?
- Does the provider keep copies of the confidential client information after the relationship is concluded or the lawyer or law firm has removed particular client information from the provider?

- What are the provider's policies and procedures regarding emergency situations such as natural disasters and power interruption?
- Where, geographically, is the server used by the provider located?

While this list is not exhaustive, it is comprehensive and provides a great starting point in researching vendors. Narrow in on two or three cloud-based or other software providers that offer the services you desire and then ask these questions. Make notes, compare, and determine which cloud service provides you with what you need to manage your practice and meet the duties owed to your clients.

NOTE While the questions provided in E-437 are directed at the evaluation of cloud-based software, lawyers could also utilize the questions as a framework for evaluating any software, IT product, or vendor to ensure they are meeting their ethical duties.

Addressing Cybersecurity Concerns

Ethics Opinion KBA E-446 states lawyers have an ethical responsibility to implement cybersecurity measures to protect client information. The opinion also states that while a lawyer cannot delegate ethical responsibilities to third parties, a lawyer should seek assistance from others when lacking sufficient information, education, and/or training to comply with the Rules.

Many lawyers will want to engage an IT provider that can assist the firm in meeting their needs in a secure environment. The firm's needs will vary based on the nature of the practice and the volume of digital files. However, basic protection measures like implementing **multifactor authentication** for access to secure data (email, the network, etc.) as well as regular data backups to multiple locations (including use of cloud backups) can be great first steps.

Lawyers should also consider obtaining cybersecurity insurance coverage which can help protect the firm from the financial costs of a breach while also mitigating issues with a rapid response from the carrier's experts. Many carriers also offer a variety of educational resources to help prevent cyber attacks.

CLIENT TRUST ACCOUNT SCAMS

Lawyers are frequently the target of scams that, if effective, result in losses in client trust accounts and violations of trust account fiduciary rules. Real estate, litigation, and wills and estate lawyers are primary targets, but all lawyers should expect a scam attempt. As of 2023, there are two common types of fraud. The first retains the firm on a contrived legal matter so that they can run a counterfeit check through the firm trust account and walk away with real money. The second uses email or other electronic communication to intervene in a legitimate case and redirect a wire transfer to their own account.

The best risk management practice with any check deposited in a client trust account is to make no disbursements on it until the funds are collected in the account, regardless of its apparent validity. Advise clients at the inception of representation in a letter of engagement that they will not receive funds until funds from any check received in payment of their matter have been collected in the trust account. When arranging for wire transfers, double- and triple-check that the source of the instruction is a legitimate party to the matter—interceptors often use spoofed email addresses that may appear the same but have one letter different (i.e., risks@lmick.com instead of the legitimate **risk@lmick.com**).

PRACTICE TIP **Scams targeting lawyers have become so pervasive that some states are considering the failure to recognize them a violation of the ethics rule on competence. The old adage "if it sounds to good to be true, it probably is" often applies. If lawyers are unsure, an internet search may be all it takes to determine whether they are being scammed. Specific websites which may be useful include the Federal Trade Commission, the Better Business Bureau, and AvoidAClaim: Claims Prevention & Practice Management for Lawyers.**

FILE RETENTION BEST PRACTICES

There is no specific requirement to retain records once a matter is closed unless the matter involved a client trust account. The Kentucky Rules of Professional Conduct require a five-year retention period for trust account records (SCR 3.130(1.15(a))). Additionally, the Kentucky Bar Association Ethics Committee provides some general guidelines in **Ethics Opinion E-436**. The opinion states it is logical to maintain the case files where a client trust account is utilized for five years, as well. The opinion goes on to point out that some files must be retained for longer than five years (e.g. claims of minor children until child reaches age of majority; tax matters as long as client liability is possible; files involving a representation in which a malpractice claim might be made.)

For more information about file retention policies, including recommendations for discussion in engagement and termination letters, review Lawyers Mutual's article on best practices for closed client file retention policies.

UNCLAIMED FUNDS

It is not unusual for a lawyer to be in possession of property belonging to a client or third party with whom the lawyer has lost contact. In these circumstances the lawyer is required to continue to safekeep this property just as any other client property. A diligent effort must be made to locate the owner and deliver the funds or non-monetary property. These efforts might include calling the client's employer, visiting last known addresses, and attempting to make contact by phone, mail, and internet. A good practice is to get key location information from the client at the time the representation is undertaken[3]. Be sure to get addresses, telephone numbers, names of people who will know where the client will be, social security numbers, drivers license numbers, and dates of birth. With impaired clients it is often helpful to get the names and numbers of professionals assisting the client with health problems (e.g., health care providers and government agencies working with the impaired client).

Unclaimed funds in an IOLTA account. **SCR 3.830(21)** allows unclaimed funds in IOLTA accounts to be remitted to the Kentucky IOLTA Fund provided that reasonable efforts, as set forth in the rule, to locate the rightful owner of the funds have been conducted. Remit unclaimed funds by completing **this form** and mailing it, along with a check for the funds, to Kentucky IOLTA Fund, 514 W. Main Street, Frankfort, KY 40601.

Unclaimed funds in a dedicated client trust account. Unlike unclaimed funds in an IOLTA account, unclaimed funds in a dedicated client trust account should escheat to the state in accordance with Kentucky's abandoned property law set forth in **KRS Chapter 393A**.

SUCCESSION AND PLANNING

It is important for lawyers to have a plan in place for how client trust funds will be handled in the event of the lawyer's death, disability, impairment, or incapacity. **KBA E-405** addresses the responsibilities of sole practitioners to plan for succession. Lawyers Mutual recommends entering into a written agreement with a back-up attorney; specific considerations and recommendations are explored in **Lawyers Mutual's Disaster Planning series found on their website**. For additional checklists, forms, and advice on succession and planning, visit the KBA website **here**.

If you find yourself as the back-up lawyer closing a practice following the death of a lawyer, Lawyers Mutual recommends taking the following steps to begin handling client trust accounts:

- Make reasonable efforts to identify all clients with funds in a trust account and provide notice of the closure
- Review trust account records and identify any unearned funds at the time of death of the lawyer
- Return any unearned funds to the client(s)
- If, after reasonable effort you are unable to locate a client with funds in an IOLTA account, consider remitting to the IOLTA Fund under SCR 3.830(21)(a)

3 Prior editions were titled *Client Trust Account, Principles & Management for Kentucky Lawyers.*

- Arrange for the maintenance of trust account records for five years
  - The recordkeeping requirements of Rule 1.15 as well as the ABA rules indicate the lawyer closing the practice has a responsibility to make these arrangements. The arrangement could be an agreement with the executor or the personal representative to keep the records for five years. However, the closing attorney may want to consider maintaining the trust account records themselves, depending on the circumstances of the closure.

KYLAP PROVIDES CONFIDENTIAL HELP

Kentucky Lawyer Assistance Program (KYLAP) provides CONFIDENTIAL assistance to all Kentucky law students, lawyers and judges with mental health issues and impairments including depression, substance use disorders, process addictions, and chronic anxiety disorders.

You may wonder what KYLAP has to do with client trust account issues? The answer is that impaired attorneys are at the greatest risk of committing trust account violations. This is true nationwide. In several studies, lawyers with gambling addictions (a process disorder) were at the highest risk of all lawyers to either misappropriate or steal client funds from their trust account. If you are an attorney with a history of gambling addiction, you can build in protections for yourself and your clients by taking simple steps like requiring two signatures on all drafts or removing yourself from financial authority within the firm. There are other safety measures to consider that will protect you if there is a return to gambling.

Lawyers with other impairments are at risk of violating the rules as well. Most of us think of an "impaired" attorney as someone with a severe alcohol or other substance use disorder who is completely unable to do anything other than drink or drug. But that's not how the Kentucky Supreme Court defines "impairment.

Kentucky Supreme Court Rule 3.900 defines "impairment" as: "any mental, psychological or emotional condition that impairs or may foreseeably impair a person's ability to practice law or serve on the bench."

The definition "any" mental health condition includes such things as severe depression and chronic anxiety. What we know about impairment is that many times the symptoms of one mimics another. For example:

SYMPTOMS OF DEPRESSION

- Missing work
- Failing to communicate with clients
- Inability to complete tasks in a timely fashion
- Last to arrive/first to leave
- Avoiding law partners/clients
- Unusually thin-skinned/short tempered

SYMPTOMS OF ADDICTION

- Missing work
- Failing to communicate with clients
- Inability to complete tasks in a timely fashion
- Last to arrive/first to leave
- Avoiding law partners/clients
- Unusually thin-skinned/short tempered

For lawyers, an inability to work (for whatever reason) generally results in an inability to generate revenue. Watch for the symptoms of depression, addiction or other mental health issues that might lead you or a colleague down a path of making bad financial decisions. For immediate anonymous online self-tests, go to **https://screening.mhanational.org/screening-tools/**.

If you find you have a mental health issue, call KYLAP and they can help in a number of ways:

- Offer you four free counseling visits to a licensed therapist through our relationship with a third-party Employee Assistance Program.
- Refer you to an in- or out-patient treatment program, a licensed therapist, or a psychiatrist who is taking new patients.
- Lend you funds to pay for mental health treatment or medications through the KYLAP Foundation, Inc., through the form of forgivable loans.

And it's **all** confidential.

For more information, check out the KYLAP website at **www.KYLAP.org** or call (502) 226-9373.

APPENDIX A: THE KENTUCKY RULES

These Kentucky Supreme Court Rules are included in the appendix for reference. These rules are subject to updates by the Kentucky legislature and Kentucky Supreme Court. For the current versions, please visit the **Kentucky Court of Justice page**.

RULE 3.130 (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, third person, or both in the event of a claim by each to the property. The separate account referred to in the preceding sentence shall be maintained in a bank which has agreed to notify the Kentucky Bar Association in the event that any overdraft occurs in the account. 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) Upon receiving funds or other property in which a client has an interest, a lawyer shall promptly notify the client. Except as stated in this Rule or otherwise permitted by law or by agreement with the client a lawyer shall promptly deliver to the client any funds or other property that the client is entitled to receive and, upon request by the client, shall promptly render a full accounting regarding such property.

(c) When in the course of representation a lawyer is in possession of funds or other property in which the lawyer and client claim interests and are not in agreement regarding those interests, the funds or other property in dispute shall be kept separate by the lawyer until the dispute is resolved. The lawyer shall promptly distribute all portions of the funds or other in which the interests are not in conflict.

(d) A lawyer may deposit the lawyer's own funds in a client trust account for the sole purpose of paying bank service charges on that account, but only in an amount necessary for that purpose.

(e) Except for advance fees as provided in 1.5(f), 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.

Comments

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, e.g., ABA Model Financial Recordkeeping Rule.

2. 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.

3. While normally it is impermissible to commingle the lawyer's own funds with client funds, paragraph (d) 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. A lawyer may deposit funds in a trust account to provide funds for restitution of the defalcation caused by others, if necessary under any legal obligation to a banking institution, client or third party whose funds have been converted.

4. Paragraph (e) requires that when a lawyer has collected an advance deposit on a fee or for expenses or a flat fee for services not yet completed, the funds must be deposited in the trust account until earned, at which time they should be promptly distributed to the lawyer. The foregoing shall not apply to advance fees as set out in 1.5(f). At the termination of the client-lawyer relationship the lawyer must return any amount held that was not earned or was an unreasonable fee, as provided by Rules 1.5 and 1.16(d).

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.

RULE 3.830: KENTUCKY IOLTA FUND

The Kentucky Bar Foundation, Inc., a nonprofit corporation, shall maintain a special fund for the purpose of depositing interest from Kentucky Bar Association members' trust accounts, as hereinafter provided, and the name of the fund shall be the Kentucky IOLTA Fund ("IOLTA").

Except as set forth in paragraph (14) of this rule, a lawyer or law firm shall create and maintain in a participating financial institution, as defined in paragraph (4) below, an interest-bearing trust account for clients' funds which are nominal in amount or to be held for a short period of time so that they could not earn interest income for the client in excess of the costs incurred to secure such income (hereinafter sometimes referred to as an "IOLTA account") in compliance with the following provisions:

(1) No funds may be deposited in any IOLTA account when either the amount or the period of time that the funds are held would earn for the client interest above the costs that would otherwise be incurred to generate such interest.

(2) No earnings from an IOLTA account shall be made available to a lawyer or law firm.

(3) An IOLTA account shall be established with a participating financial institution (i) authorized by federal or state law to do business in Kentucky, and (ii) insured by the Federal Deposit Insurance Corporation or its equivalent. Funds in each IOLTA account shall be subject to withdrawal upon request and without delay and without risk to principal by reason of said withdrawal.

(4) Participating financial institutions that maintain IOLTA accounts shall pay on the accounts the highest interest rate or dividend generally available from the institution to its non-IOLTA account customers when IOLTA accounts meet or exceed the same minimum balance or other account eligibility qualifications. In determining the highest interest rate or dividend generally available from the institution, participating financial institutions may consider factors, in addition to the IOLTA account balance, that are customarily considered by the institution when setting interest rates or dividends for its non-IOLTA customers. Such factors should not discriminate between IOLTA accounts and accounts of non-IOLTA customers. All interest earned net of fees or charges shall be remitted to IOLTA, which is designated in paragraph (16) of this rule to organize and administer the IOLTA program, and the depository participating institution shall submit reports thereon as set forth below.

(5) A participating financial institution may satisfy the comparability requirements set forth in paragraph (4) above by electing one of the following options:

(i) Pay an amount on funds that would otherwise qualify for the investment options equal to 70% of the federal funds targeted rate as of the first business day of the month or other IOLTA remitting period, which is deemed to be already net of allowable reasonable service charges or fees. The foregoing option of paying 70% of the federal funds targeted rate shall only apply when such rate is established in the range of 1.0% to 4.0% unless otherwise agreed to by IOLTA and the participating financial institution.

(ii) Pay a yield rate specified by IOLTA, if IOLTA so chooses, which is agreed to by the participating financial institution. The rate would be deemed to be already net of allowable reasonable fees and would be in effect for and remain unchanged during a period of no more than twelve months from the inception of the agreement between the financial institution and IOLTA.

(6) IOLTA accounts may be established as:

(i) An interest-bearing checking account such as a negotiable order of withdrawal account;

(ii) a checking account with an automated investment feature, such as an overnight and investment in repurchase agreements or money market funds invested solely in or fully collateralized by U.S. Government Securities, including U.S. Treasury obligations and obligations issued or guaranteed as to principal and interest by the United States or any agency or instrument thereof;

(iii) a checking account paying preferred interest rates, such as money market or indexed rates;

(iv) any other suitable interest-bearing deposit account offered by the institution to its non-IOLTA customers.

(7) A daily financial institution repurchase agreement shall be fully collateralized by United States Government Securities and may be established only with an eligible 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 shall be invested solely in United States Government Securities or repurchase agreements fully collateralized by United States Government Securities, shall 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, the money market fund shall have total assets of at least two hundred fifty million dollars ($250,000,000).

(A) Nothing in this rule shall preclude a participating financial institution from paying a higher interest or dividend than described above or electing to waive any service charges or fees on IOLTA accounts.

(B) Interest and dividends shall be calculated in accordance with the participating financial institution's standard practice for non- IOLTA customers.

(C) Allowable reasonable service charges or fees may be deducted from interest or dividends on an IOLTA account only at the rates and in accordance with the customary practices of the eligible institution for non-IOLTA customers. No fees or service charges other than allowable reasonable fees may be assessed against the accrued interest or dividends on an IOLTA account.

(D) Any IOLTA account which has or may have the net effect of costing IOLTA more in fees than earned in interest over a period of any time, may, at the discretion of IOLTA, be exempted from and removed from the IOLTA program. Exemption of an IOLTA account from the IOLTA program revokes the permission to use IOLTA's tax identification number for that account. Exemption of such account from the IOLTA program shall not relieve the lawyer and/or law firm from the obligation to maintain the property of client funds separately, as required above, in a trust account and also will not relieve the lawyer of the annual IOLTA certification.

(8) Lawyers or law firms depositing client funds in an IOLTA account established pursuant to this rule shall, on forms approved by IOLTA, direct the depository institution:

(A) to remit all interest or dividends, net of reasonable service charges or fees, if any, on the average monthly balance in the account, or as otherwise computed in accordance with the institution's standard accounting practice, at least quarterly, solely to IOLTA. The depository institution may remit the interest or dividends on all of its IOLTA accounts in a lump sum; however, the depository institution must provide, for each individual IOLTA account, the information to the lawyer or law firm and to IOLTA required by subparagraphs (8)(B) and (8)(C) of this rule;

(B) to transmit with each remittance to IOLTA a statement showing the name of the lawyer or law firm for whom the remittance is sent, the rate of interest applied, average daily balance, service charges, if any, and such other information as is reasonably required by IOLTA;

(C) to transmit to the depositing lawyer or law firm a periodic account statement for the IOLTA account reflecting the amount of interest paid to IOLTA, the rate of interest applied, the average account balance for the period for which the interest was earned, and such other information as is reasonably required by IOLTA; and

(D) to waive any reasonable service charge that exceeds the interest earned on any IOLTA account during a reporting period ("excess charge").

(9) The IOLTA program will issue refunds when interest has been remitted in error, whether the error is the bank's or the lawyer's. Requests for refunds must be submitted in writing by the bank, the lawyer, or the law firm on a timely basis, accompanied by documentation that confirms the amount of interest paid to the IOLTA program. As needed for auditing purposes, the IOLTA program may request additional documentation to support the request. The refund will be remitted to the appropriate financial institution for transmittal at the lawyer's direction after appropriate accounting and reporting. In no event will the refund exceed the amount of interest actually received by the IOLTA program.

(10) All interest transmitted to IOLTA shall be held, invested and distributed periodically in accordance with a plan of distribution which shall be prepared by IOLTA and approved at least annually by the Supreme Court of Kentucky, for the following purposes:

(A) to pay or provide for all costs, expenses and fees associated with the administration of the IOLTA program;

(B) to establish appropriate reserves;

(C) to assist or help establish approved legal services and pro bono programs;

(D) or such other law-related programs for the benefit of the public as are specifically approved by the Supreme Court from time to time.

(11) The information contained in the statements forwarded to IOLTA under paragraph (8)(B) of this rule shall remain confidential, and the provisions of any other Supreme Court Rules providing for confidentiality are not hereby abrogated; therefore, IOLTA shall not release any information contained in any such statement other than as a compilation of data from such statements, except as directed in writing by the Supreme Court.

(12) IOLTA shall have full authority to and shall, from time to time, prepare and submit to the Supreme Court for approval, forms, procedures, instructions and guidelines necessary and appropriate to implement the provisions set forth in this rule and, after approval thereof by the Court, shall promulgate same.

(13) On or before September 1 of each year, every lawyer admitted to practice in Kentucky shall certify to IOLTA, in such form as IOLTA shall provide ("IOLTA Certification Form"), that the member is in compliance with, or is exempt from, the provisions of this rule. The IOLTA Certification Form shall include the participating financial institution, account numbers, name of law firm or lawyer accounts and such other information as IOLTA shall require. If the lawyer is exempt from the IOLTA program, the lawyer must still submit an IOLTA Certification Form annually to certify to IOLTA that the lawyer is exempt from the provisions in this rule. Each lawyer shall keep and maintain records supporting the information submitted in the IOLTA Certification Form. The lawyer shall maintain these records for a period of three years from the end of the period for which the IOLTA Certification Form is filed, and these records shall be submitted to IOLTA upon written request.

14.The lawyer is exempt from this rule if:

(A) not engaged in the private practice of law;

(B) does not have a trust account in a financial institution within the Commonwealth of Kentucky;

(C) serving full time as a judge, attorney general, public defender, U.S. attorney, commonwealth attorney, county attorney, on duty with the armed services or employed by a local, state or federal government, and is not otherwise engaged in the private practice of law;

(D) is a corporate counsel or teacher of law and is not otherwise engaged in the private practice of law;

(E) has been exempted by an order of general or special application of this Court which is cited in the certification;

(F) compliance with Rule 3.830 would work an undue hardship on the lawyer or would be extremely impractical, based on the geographic distance between the lawyer's principal office and the closest participating financial institution, or on other compelling and necessary factors; or

(G) does not manage or handle client trust funds.

(15) The determination of whether a client's funds are nominal or short-term so that they could not earn income in excess of costs shall rest in the sound judgment of the lawyer or law firm. No lawyer shall be charged with an ethical impropriety or other breach of professional conduct based on the good faith exercise of such judgment.

(16) IOLTA is hereby designated as the entity to organize and administer the program established by this rule in accordance with the following provisions:

(A) The determination of whether or not a financial institution is a participating institution as defined in paragraph (4) above, and whether it is meeting the requirements of this rule shall be made by IOLTA. IOLTA shall maintain a list of participating financial institutions, and shall provide a copy of the list to any Kentucky lawyer upon request.

(B) Lawyers may only maintain IOLTA accounts in participating financial institutions. Participating financial institutions are those that voluntarily offer IOLTA accounts and comply with the requirements of this rule. If a financial institution becomes non-participatory, the lawyer or law firm must move its IOLTA account to a participating financial institution as described in paragraph (4) above, upon ninety (90) days written notice by IOLTA, and recertify to IOLTA the transfer.

(17) If the IOLTA Certification Form is timely filed, indicating compliance, there will be no acknowledgment. Should an IOLTA Certification Form not be filed by a lawyer or if filed, fail to evidence compliance, IOLTA shall contact the lawyer and attempt to resolve the non-compliance administratively.

(18) Lawyers licensed in Kentucky must notify IOLTA in writing within thirty (30) days of any change in IOLTA status, including the opening or closing of any IOLTA accounts, except as provided in paragraph (16)(B) above.

(18) For the purpose of administering the funds deposited in the Kentucky IOLTA Fund, the Kentucky Bar Foundation is authorized to create a separate Board of Trustees to administer this fund, which shall consist of ten (10) members of the Association. One (1) member will be from each of the seven (7) Supreme Court Districts of the Commonwealth. The remaining three (3) members will be the Chief Justice of the Supreme Court of Kentucky, the President of the Kentucky Bar Association and the Chair of the Kentucky Bar Foundation, or a member of the Association appointed by each of such persons. These three (3) persons will serve year to year at the pleasure of the appointing person.

(A) Members of the Board of Trustees from the Supreme Court Districts shall be appointed by the Board of Governors of the Kentucky Bar Association and approved by the Supreme Court. Appointments shall be made for a three-year term. Members may be reappointed, but no member shall serve more than two (2) successive three-year terms. Each member shall serve until a successor is appointed and qualified. Vacancies occurring through death, disability, inability, or disqualification to serve, or by resignation, shall be filled for the remainder of the vacant term in the same manner as the initial appointments are made by the Court. The members of the Board of Trustees of the Kentucky IOLTA Fund shall serve without compensation, but shall be paid their reasonable and necessary expenses incurred in the performance of their duties. The staff support for the Board of Trustees shall be paid by IOLTA.

(B) The IOLTA Board of Trustees (the "Trustees") shall have general supervisory authority over the administration of the IOLTA program, subject to the continuing jurisdiction of the Supreme Court.

(C) The Trustees shall receive the net earnings from IOLTA accounts established in accordance with this rule and shall make appropriate temporary investments of IOLTA program funds pending disbursement of such funds.

(D) The Trustees shall, by grants, appropriations and other appropriate measures, make disbursements from the IOLTA program funds, including current and accumulated net earnings, in accordance with the plan of distribution approved by the Supreme Court on at least an annual basis.

(E) The Trustees shall maintain proper records of all IOLTA program receipts and disbursements, which records shall be audited or reviewed annually by a certified public accountant approved by the Supreme Court.

(F) The Trustees shall be indemnified by IOLTA against any liability or expense arising directly or indirectly out of the good faith performance of their duties.

(G) The Trustees shall present an annual administrative budget request to the Board of Governors for their approval, after which the budget shall be forwarded to the Supreme Court for approval. Staff for the operation of IOLTA shall be under the supervision and responsible to the Executive Director of the Bar Association.

(H) The Trustees shall monitor attorney compliance with the provisions of this rule and will report to the Supreme Court those attorneys not in compliance.

(I) In the event the IOLTA program or its administration by IOLTA is terminated, all assets of the IOLTA program, including any program funds then on hand, shall be transferred in accordance with the Order of the Supreme Court terminating the IOLTA program or its administration by IOLTA; provided, such transfer shall be to an entity which will not violate the requirements IOLTA must observe regarding transfer of its assets in order to retain its tax-exempt status under the Internal Revenue Code of 1986, as amended, or similar future provisions of law.

(20) If the Kentucky IOLTA Fund receives residual funds as provided in Civil Rule 23.05(6), it shall deposit those funds into the Civil Rule 23 Account, an interest-bearing account maintained in a banking institution within the Commonwealth of Kentucky. Those funds are to be timely disbursed, in their totality, to the four Kentucky Civil Legal Aid Organizations in accordance with the current poverty formula established by the Legal Services Corporation in Washington, D.C. The Kentucky IOLTA Fund shall report to the Kentucky Supreme Court annually, on the first business day of September, regarding the status of the Civil Rule 23 Account, including all receipts and disbursements during the preceding year.

(21)

(A) If a lawyer does not know the identity or the location of the owner of funds held in the lawyer's IOLTA account, or the lawyer discovers that the owner of the funds is deceased, the lawyer must make reasonable efforts to identify and locate the owner or the owner's heirs or personal representative. If, after making such efforts, the lawyer cannot determine the identity or the location of the owner, or the owner's heirs or personal representative, the lawyer shall either continue to hold the unclaimed funds in an IOLTA account, or remit the unclaimed funds to the Kentucky IOLTA Fund in accordance with written procedures published by the Kentucky IOLTA Fund and available through its website or upon request.

(B) A lawyer remitting unclaimed funds to the Kentucky IOLTA Fund shall keep a record of the remittance that includes the name and last known address of the owner of the funds, if the owner of the funds is known; the date of death of the deceased owner; the efforts made to identify and locate the owner of the funds or deceased owner's heirs, or personal representatives; the amount of funds remitted; the period of time during which the funds were held in the lawyer's or law firm's IOLTA account; and the date the funds were remitted.

(C) If, after remitting unclaimed funds to the Kentucky IOLTA Funds, the lawyer determines the identity and the location of the owner or the owner's heirs or personal representative, the lawyer shall request a refund for the benefit of the owner or the owner's estate in accordance with written procedures that the Kentucky IOLTA Fund shall publish and make available through its website or upon request.

(D) What constitutes reasonable efforts, as set out in paragraph (A), would depend on whether the lawyer knows the identity of the owner of certain funds held in the IOLTA account, or the lawyer knows the identity of the owner of the funds, but not the owner's location or the location of the deceased owner's heirs or personal representative. When the lawyer does not know the identity of the owner of the funds or the deceased owner's heirs or personal representative, reasonable efforts shall include an audit of the IOLTA account to determine how and when the funds lost their association to a particular owner or owners, and whether they constitute attorney's fees earned by the lawyer or expenses to be reimbursed to the lawyer or third person. When the lawyer knows the identity, but not the location of the owner of the funds, or the location of the owner's heirs or personal representative, reasonable efforts shall include attempted contact using last known contact information, reviewing the file to identify and contact third parties who may know the location of the owner or the owner's heirs or personal representative, or conducting internet searches. After making reasonable, but unsuccessful efforts in identifying and locating the owner of the funds or the owner's heirs or personal representative, a lawyer's decision to continue to hold the funds in the IOLTA account, as opposed to remitting the funds to the Kentucky IOLTA fund, does not relieve the lawyer of the obligation to maintain records pursuant to paragraph (B), or to determine whether it is appropriate to maintain the funds in an IOLTA account.

APPENDIX B: ABA MODEL RULE ON FINANCIAL RECORD KEEPING

Adopted by the American Bar Association House of Delegates on February 9, 1993
Incorporated into the Kentucky Rules of Professional Conduct in Rule 1.15, Comment 1.

PREFACE

Rule 1.15 specifically requires a lawyer to preserve "complete records" with respect to a law firm's trust accounts. It also obligates a lawyer to "promptly render a full accounting" for the receipt and distribution of trust property. A violation of Rule 1.15 may subject a lawyer to professional discipline. Rule 1.15 does not, however, provide lawyers or law firms with practical guidance in complying with these fiduciary obligations or in establishing basic accounting control systems for their law practices.

The Model Rule on Financial Recordkeeping is intended to give further definition to the requirements of Rule 1.15. Adapted from existing court rules, it proposes uniform and minimal standards for the maintenance of law firm financial records. These standards should guide lawyers and law firms, particularly those new to the practice of law.

THE RULE

A. A lawyer who practices in this jurisdiction shall maintain current financial records as provided in this rule, and shall retain the following records for a period of [five years] after termination of the representation:

1. receipt and disbursement journals containing a record of deposits to and withdrawals from bank accounts which concern or affect the lawyer's practice of law, specifically identifying the date, source, and description of each item deposited, as well as the date, payee and purpose of each disbursement;

2. ledger records for all trust accounts required by [Rule 1.15 of the ABA Model Rules of Professional Conduct], showing, for each separate trust client or beneficiary, the source of all funds deposited, the names of all persons for whom the funds are or were held, the amount of such funds, the descriptions and amounts of charges or withdrawals, and the names of all persons to whom such funds were disbursed;

3. copies of retainer and compensation agreements with clients [as required by Rule 1.5 of the ABA Model Rules of Professional Conduct];

4. copies of accountings to clients or third persons showing the disbursement of funds to them or on their behalf;

5. copies of bills for legal fees and expenses rendered to clients;

6. copies of records showing disbursements on behalf of clients;

7. checkbook registers or check stubs, bank statements, records of deposit, and prenumbered canceled checks or their equivalent;

8. copies of [monthly] trial balances and [quarterly] reconciliations of the lawyer's trust accounts; and

9. copies of those portions of clients' files that are reasonably necessary for a complete understanding of the financial transactions pertaining to them.

B. With respect to trust accounts required by [Rule 1.15 of ABA the Model Rules of Professional Conduct]:

1. only a lawyer admitted to practice law in this jurisdiction shall be an authorized signatory on the account;

2. receipts shall be deposited intact and records of deposit should be sufficiently detailed to identify each item; and

3. withdrawals shall be made only by check payable to a named payee and not to cash, or by authorized bank transfer.

C. Records required by this rule may be maintained by electronic, photographic, computer or other media provided that they otherwise comply with this rule and provided further that printed copies can be produced. These records shall be located at the lawyer's principal office in the jurisdiction or in a readily accessible location.

D. Upon dissolution of any partnership of lawyers or of any legal professional corporation, the partners or shareholders shall make appropriate arrangements for the maintenance of the records specified in Paragraph A of this rule.

E. Upon the sale of a law practice, the seller shall make appropriate arrangements for the maintenance of the records specified in Paragraph A of this rule.

Comment

[1] Paragraph A enumerates the basic financial records that a lawyer should maintain with regard to the business and trust accounts of a law firm. These include the standard books of account, and the supporting records which are necessary to safeguard and account for the receipt and disbursement of client funds as required by Rule 1.15 of the ABA Model Rules of Professional Conduct or its equivalent. Consistent with Rule 1.15, this rule proposes that lawyers maintain financial and safekeeping records for a period of five years after termination of each particular legal engagement or representation.

[2] The potential of these records to serve as safeguards is realized only if the procedures set forth in Paragraph A(8) are regularly performed. The trial balance is the sum of balances of each client's ledger card (or the computerized equivalent). Its value lies in comparing it on a monthly basis to a control balance. The control balance starts with the previous month's balance, then adds receipts from the Trust Receipts Journal and subtracts disbursements from the Trust Disbursements Journal. Once the total matches the trial balance, the reconciliation readily follows by adding amounts of any outstanding checks and subtracting any deposits not credited by the bank at month's end. This balance should agree with the bank statement. Quarterly reconciliation is recommended only as a minimum requirement; monthly reconciliation is the preferred practice given the difficulty of identifying an error (whether by the lawyer or the bank) among three months' transactions.

[3] Paragraph B enumerates minimal accounting controls for lawyer trust accounts. It also enunciates the requirement that only a lawyer admitted to the practice of law in the jurisdiction be an authorized signatory on a lawyer trust account.

[4] Paragraph C allows the use of alternative media for the maintenance of bookkeeping records if printed copies of necessary reports can be produced. If trust records are computerized, a system of regular and frequent (preferably daily) back-up procedures is essential.

[5] Paragraph D and E provide for the preservation of a lawyer's financial records in the event of dissolution or sale of a law practice.

APPENDIX C:
RECORDKEEPING EXAMPLES

CHOOSING THE RIGHT RECORDKEEPING METHOD

Lawyers should maintain both the client trust account journal and the client trust account ledger.

THE JOURNAL

The client trust account journal tracks all the transactions in an account: all deposits and withdrawals, including payment of bank fees. The ABA Model Rule on Financial Recordkeeping only requires the use of the journal for dedicated client trust accounts. However, this overall record should be maintained for every client trust account, both dedicated and pooled accounts. This allows lawyers to easily track every transaction for the account(s) in a single format.

The ABA Model Rule requires the journal record to include:

- *Record of deposits of funds, including date, source, description of each*
- *Record of disbursements, including date, payee, and purpose of each disbursement*

Example

Jones & Jones Pooled Client Trust Account

Number: 123456
Bank: PN-ONE

DATE	CHECK # ACCOUNT	CLIENT SUB SOURCE MEMO	PAYEE CHARGE AMOUNT	CHECK / AMOUNT	DEPOSIT	BALANCE
8/1/23			Beginning of month balance			$50,000
8/2/23	123	Doaks 07-987	Dr. Smith payment	$500		$49,500
8/2/223		Shelby 08-654	State Farm settlement		$30,000	$79,500
8/9/23	124	Shelby 08-654	Settlement check to client	$20,000		$59,500
8/9/23	125	Shelby 06-654	Firm fee	$10,000		$49,500
8/15/23		Bank fees	Check printing	$30		$49,470
8/25/23		Bank fees	Quarterly fee	$40		$49,430
8/29/23		Bank fees funds	Firm replenish		$70	$49,500
8/31/23			End of month balance			$49,500

THE LEDGER

The client trust account ledger focuses specifically on tracking a client's balance by recording client fund transactions. This ledger should be maintained for every client but is particularly important for clients with funds in a pooled trust account. Also, if funds are being kept in the trust account to cover bank charges, a "client" ledger should be kept to track those funds as well.

While the ABA model rule only requires a monthly client balance, current software and regular input of transactions should allow a lawyer to pull client balances more frequently.

The ABA Model Rule requires the ledger to include:

- *Source of all funds deposited*
- *Owner of funds*
- *Amount of funds, at least monthly*
- *Description and amounts of deposits and withdraws*
- *Names of persons receiving disbursements*

NOTE A copy of the client ledger is often used by lawyers as an accounting to the client. This dual purpose should be considered when designing the format of client ledgers and when making explanatory entries in the ledgers. For example, the names of court reporters and medical records companies will not be familiar to clients, therefore, additional explanation is necessary for an understanding by the client of how funds were spent.

Example

Client Name/File Number: Jim Davis — File# 2009 –12345

Matter/Adverse Party: Auto crash injury — Joe Doe

DATE	Transaction / Memo	CHECK #	DISBURSEMENT	DEPOSIT	BALANCE
8/1/23	Beginning Balance				$1,750
8/3/23	AIG settlement			$50,000	$51,750
8/8/223	Memorial Hospital – surgery 7/9/04	121	$20,000		$31,750
8/8/23	Settlement proceeds to client	122	$20,000		$11,750
8/9/23	Firm fees	123	$10,000		$1,750

MONTHLY CLIENT TRUST ACCOUNT RECONCILIATION REPORT

All client trust account checkbook registers, journals, and ledgers should be reconciled monthly when bank statements are received and never less frequently than quarterly. The monthly reconciliation report is particularly important for pooled client trust accounts. The report must show that the client ledgers balance with the account journal and that the account journal balances with the bank statement. The steps in reconciling pooled accounts are shown below.

MONTHLY POOLED CLIENT TRUST ACCOUNT RECONCILIATION REPORT

For the month of: _____

1. Client ledger balances:	Totals
Client A	_____
Client B	_____
Client C	_____
Etc.	_____
2. Client Trust Account Journal balance *	*_____
3. Account bank statement balance	
(-) outstanding checks:	_____
	_____
	_____
	_____
(+) unlisted deposits:	_____
	_____
	_____
6. Bank statement reconciled balance *	*_____

** The ledgers balance, account journal balance, and reconciled bank statement balance all must be the same.*

APPENDIX D:
RELEVANT KBA ETHICS OPINIONS

- Attorney's responsibility in protecting client information and property from cyberattacks. (**KBA E-446**)
- Use of Cloud Computing for protecting client property. (**KBA E-437**)
- Retention and Disposal of Closed Client Files. (**KBA E-436**)
- Obligations of a lawyer who has funds or property belonging to a client who cannot be located. (**KBA E-433**)
- Master Commissioners IOLTA accounts for transactions related to their duties. (**KBA E-413**)
- Succession planning for sole practitioners. (**KBA E-405**)
- Withdrawal of funds received from third parties when fees are in dispute. (**KBA E-292**)
- Attorneys may not invest client funds in new accounts and use the interest to help pay the expense of accounting for the client escrow accounts. (**KBA E-126**)
- Use of credit cards for payment of earned and unearned attorney fees (**KBA E-426**)