



Trusting Client Trust Accounts – Ethical Dilemmas

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Presented by:

June D. Coleman
Messer Strickler Burnette, Ltd.

June D. Coleman



June D. Coleman, Managing Attorney for the California Office of Messer Strickler, Ltd., is a defense litigator with more than 25+ years of experience. Her areas of emphasis include defense of consumer rights actions involving the FDCPA, TCPA, and FCRA. She has a deep understanding of permissible debt collection conduct and how best to defend claims and minimize liability in the collection industry. She also defends collection attorneys before the California State Bar. Since 2008, Ms. Coleman has been voted by her peers as one of the top lawyers practicing in Northern California and Sacramento. Ms. Coleman has also been recognized by Accounts Recovery as one of the leading attorneys in the collections field for her defense work. Ms. Coleman is a Martindale Hubbell AV Preeminent rated attorney.

JColeman@MesserStrickler.com



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AGENDA



TRUST ACCOUNTS

- Client Trust Accounting 101
- Opening a Client Trust Account
- Key Concepts
- Your Trust Account Ins and Outs

CLIENT
TRUST
ACCOUNTING
101





1. Client trust accounting is a mysterious, complicated process that requires years of training and innate mathematical ability.

2. “Maintaining a client trust account” simply means opening a bank account and depositing clients' funds into it.



Client:

These duties arise in the context of an attorney-client relationship, regardless of whether you are paid for your services, and are as inviolable as your duty to maintain client confidences. These duties may also be owed to third parties.

Trust:

The willingness of people to trust a complete stranger with money just because the stranger is an attorney is a fundamental aspect of the attorney-client relationship, and maintaining that trust is the duty of every individual attorney and a matter of supreme public interest.





Accounting:

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

IOLTA accounts are depositories for funds that are nominal or held for such a short term that they would ordinarily generate less interest than would cover the bank's cost to earn that interest. Under the IOLTA rules, these funds are grouped, and the resulting interest is used to fund law-related public interest programs. State bar associations and the bank automatically transfer the interest to the state bar association or related entity to fund public interest programs, such as providing legal services to the indigent.

Law firms and lawyers generally have an IOLTA account, where trust funds are maintained for several clients.



Client Ledger

This is a written ledger for each client that details every monetary transaction on behalf of that client or other person. If you have a common client trust bank account in which the funds of more than one person are deposited, this is where you keep track of individual persons' money.

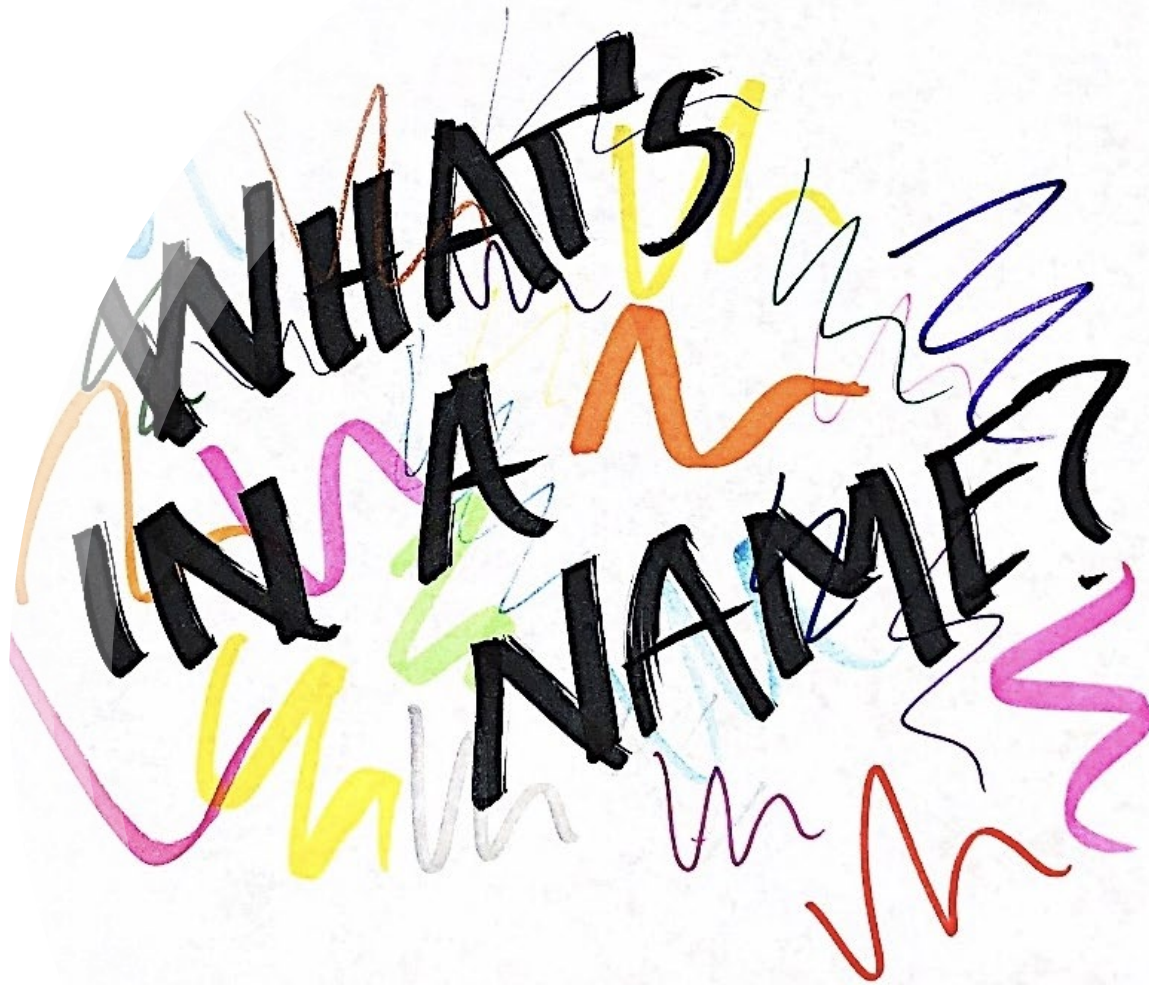
Account Journal

This is a written journal for each client trust bank account. This is where you keep track of the money going in and out of a client trust bank account.

When you have a bank account that's designated solely for one person's money, the account journal will be identical to the client ledger.

Reconciliation

You must keep a written record showing that every month you “reconciled” or balanced the account journals you keep for each client trust bank account against the client ledgers you keep for each person and the cancelled checks and bank statements for those accounts.



And Other
Concerns When
Opening a Client
Trust Account

Depending on your state's bar association rules, the account has to be designated:

1. an Attorney Trust Account,
 2. a Client Trust Account or
 3. A Client Escrow Account.
- That designation should appear on any checks or deposit slips.
 - Be sure to check with your local state bar association as to what the preference or requirement is for naming your trust account.

Should the account name be:

The managing partner at the firm

The law firm

The client or clients' name(s)

Ultimately, all trust accounts should be in the name of an attorney or the firm.** Generally, trade names cannot be used on trust accounts.

Location of account



- If you operate in different states, check each state's rules about where the account should be located . Many states require that accounts that hold trust funds for matters or clients in a state to be located in that state.
 - There may be exceptions to this rule, potentially with client consent.
- Check you state bar rules to determine if there is an approved list of banks for an IOLTA account.

- Limit accessibility of funds
- Should NOT have ATM access
- In some states, may include automatic overdraft protection in some situations
- Do not carry blank client trust bank account checks
- Who should sign your client trust account checks?

KEY CONCEPTS



SEPARATE CLIENTS ARE SEPARATE ACCOUNTS

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



ACCOUNTS


YOU CAN'T SPEND WHAT YOU DON'T HAVE

Each client has only his or her own funds available to cover their expenses, no matter how much money belonging to other clients is in your common client trust bank account. Your common client trust bank account might have a balance of \$100,000, but if you are only holding \$10.00 for a certain client, you can't write a check for \$10.50 on behalf of that client without using some other client's money.

Quote of the day!

"NEVER **SPEND** YOUR MONEY
BEFORE YOU **HAVE** IT."

THOMAS JEFFERSON



Client A	\$1,000
Client B	\$2,000
Client C	\$1,500
Client D	<u>\$ 500</u>
Total	\$5,000

YOU CAN'T PLAY THE GAME UNLESS YOU KNOW THE SCORE

KNOW
— THE —
SCORE

The “running balance” is the score. A “running balance” is the amount you have in an account after you add in all the deposits (including interest earned, etc.) and subtract all the money paid out (including bank charges for items like wire transfers, etc.). In other words, the running balance is what's in the account at any given time. The running balance for each client is kept on the client ledger, and the running balance for each client trust bank account is kept on the account journal.

THERE'S NO SUCH THING AS A “NEGATIVE BALANCE”

Checking

-\$743.89

Available balance

A “negative balance” is at best a sign of negligence and, at worst, a sign of theft. (Don't think that because you have “automatic overdraft protection” on your client trust bank account and the check doesn’t bounce, you have fulfilled your client trust account responsibilities. In client trust accounting, there are only three possibilities:

- You have a positive balance (while you are holding money for a client)
- You have a zero balance (when all the client's money has been paid out)
- You have a balance of less than zero (a so-called “negative balance”) and a problem.

TIMING IS EVERYTHING

It takes anywhere from a day to several weeks after you make a deposit before the money becomes “available for use.” A client's funds aren't “available” for you to use on the client’s behalf until they have cleared the banking process and been credited by the bank to your client trust bank account. If you write a check for a client at any time before that client's funds clear the banking process and are credited to your client trust bank account, you will be using other clients' money to cover the check.





THE FINAL SCORE IS ALWAYS ZERO

- The goal in client trust accounting is to make sure that every dollar you receive on behalf of a client is ultimately paid out. What comes in for each client must equal what goes out for that client; no more, no less.
- Many attorneys have small, inactive balances in their client trust bank accounts. Whatever the reason, as long as the money is in your client trust bank account, you are responsible for it.
- The longer these funds stay in the bank, the harder it is to account for them. Therefore, you should take care of those small, inactive balances as soon as possible, including, if necessary, following up with payees to find out why a check hasn't cleared.

ALWAYS MAINTAIN AN AUDIT TRAIL

AUDIT TRAIL



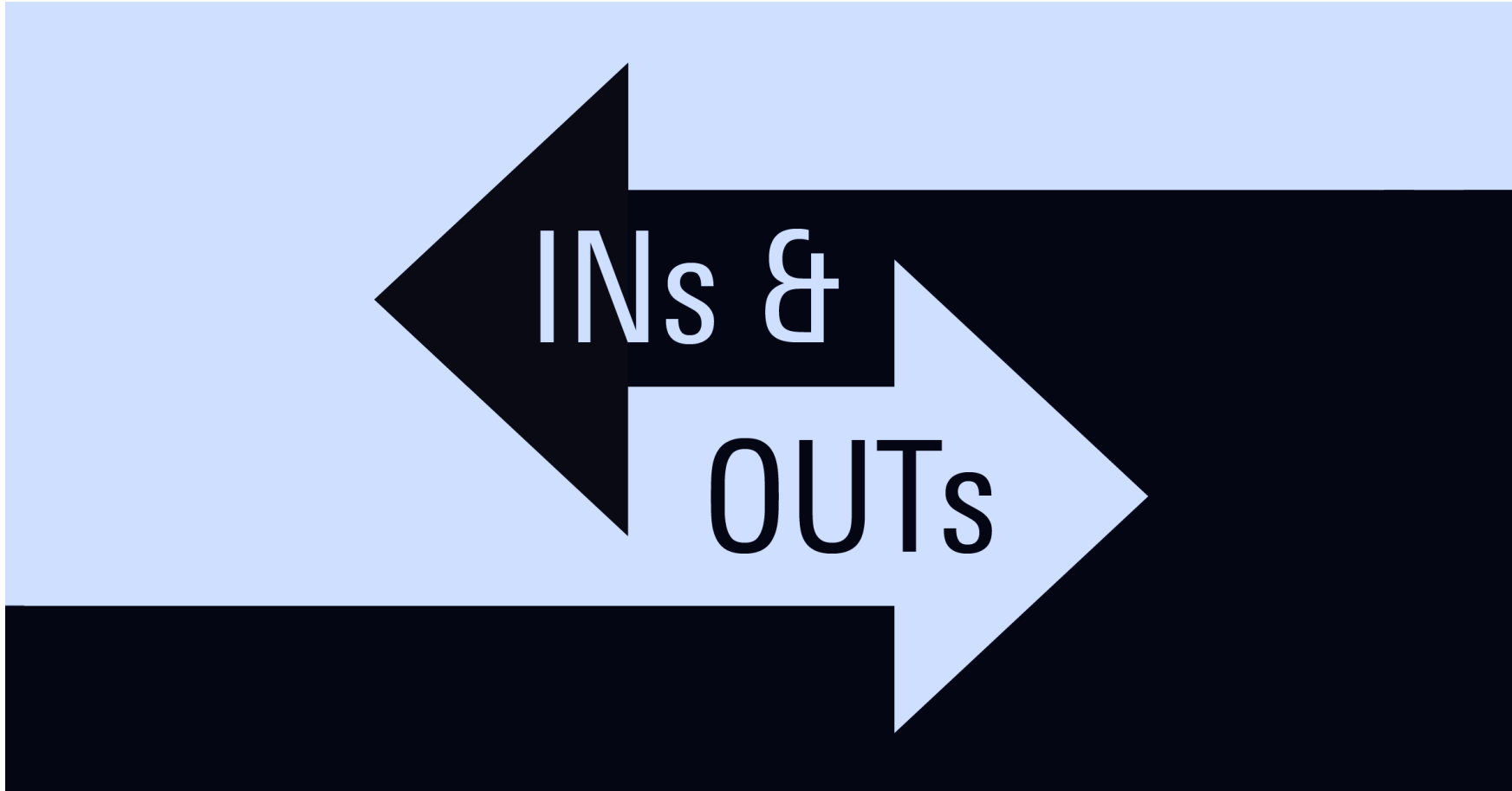
An “audit trail” is the series of bank-created records, like cancelled checks, bank statements, etc., that make it possible to trace what happened to the money you handled. An audit trail should start whenever you receive funds on behalf of a client and should continue through the final check you issue against them. Without an audit trail, you have no way to show that you have taken proper care of your clients' money, or to explain what you did with the money if any questions come up.

- Initial deposit slip
- Checkbook stub for payments
- Bank statements reflecting deposit and payments
- Cancelled checks
- Deposited checks, front and back

Reporting and Other Duties

- May need to report when you open or close an IOLTA account and register your trust accounts with your State Bar.
- May need to confirm you are complying with your trust accounting obligations. In California, most attorneys must complete an annual self-assessment questionnaire to confirm compliance and provide the questionnaire to the State Bar.
- Reconcile your client ledgers and account journal every month and maintain a written record that you did so according to California law. Cal. R. of Prof. Cond. 1.15(d)(3), (e).
- You may have a deadline to notify your client that you received money on behalf of a client. Absent good cause, in California, that deadline is within 14 days after receipt of funds.

YOUR TRUST ACCOUNT



What Monies Go into a Trust Account

Any money received for the benefit of the client must be deposited into the client trust account and cleared before it can be paid out. This includes:

- Retainers
- Money that belongs to the client outright, such as monies collected from debtors
- Settlement proceeds where a portion of the settlement funds belong to the attorney and a portion belongs to the client

Do Not Put the Following into Your Trust Account – This Would Be Commingling:

- Your Personal Funds
- Employee Payroll Taxes

What Monies Can Be Paid out of a Trust Account

You can make any payments on behalf of your client out of your client trust bank account, including paying:

- Client costs and expenses (e.g., court filing fees or deposition transcript costs)
- Disbursing settlement proceeds
- Paying yourself earned and undisputed legal fees, etc. - promptly
- You may also pay bank charges for the account.

Do Not Pay the Following out of Your Trust Account:

- Your Own Expenses, Business or Personal
- Employee Payroll Taxes
- Disputed Legal Fees

When Do You Make Payments from Your Trust Account?

- Generally, you must “promptly distribute any undisputed funds or property in the possession of the lawyer or law firm that the client or other person is entitled to receive.” Cal. R. of Prof. Cod. 1.15(d)(7).
- Some states required disbursement upon request.
- Some states have time limits. California requires distribution of undisputed funds within 45 days of receipt of funds, absent good cause.
 - Disputes could involve medical liens, statutory liens, prior attorney liens, interpleader action

Check with your state bar to determine if there are different requirements.

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