UH OH!! IOLTA ACCOUNTS AND ESCROW ACCOUNTS
By James Bolan, Esq.

It goes without saying that all lawyers reconcile their bank accounts, except for those who don't!!! In the course of our practice advising and representing lawyers and law firms (from solo practitioners to 1000+ lawyer firms), issues regularly arise as to the handling and management of funds, including IOLTA and escrow funds - they are not always the same! Many lawyers, including real estate practitioners, have never reconciled their accounts and have been living off the "float" as their practices matured. Indeed, more Board of Bar Overseers issues arise in conveyancing work than in any other endeavor, generally because of the volume of work, handling wired funds, delays inherent in securing discharges and escrows or hold-backs, as a result of which checks can remain in the financial ether for years.

To complicate matters, many lawyers amalgamate escrow funds with client/trust funds rather than setting up separate escrow accounts. An escrow account should be treated quite separately. It is usually a bank account held in the name of the depositor and an escrow agent, that is returnable to the depositor or paid to a third person on the fulfillment of an escrow condition. But, an escrow agreement consists of the delivery of money or other valuable object by one party and a promise by the other to hold it until the performance of a condition or the happening of a certain event. *Childs v. Harbor Lounge of Lynn, Inc.*, 357 Mass. 33, 35 (1970). There need not be an express writing signed by the parties. *Kaarela v. Birkhead*, 33 Mass.App.Ct. 410, 412 (1992). "It is 'the intention of the parties at the time of deposit [with the agent that] is controlling.' " *Id*. at 413, quoting *Progressive Iron Works Realty Corp. v. Eastern Milling Co.*, 155 Me. 16, 20 (1959). See, also *Aranha v. Eagle Fund, Ltd*., 245 B.R. 1 (Bankr. D. Mass. 2000); *Mercurius Inv. Holding, Ltd v. Aranha, et. al*., 247 F.3d 328 (2001).

For numerous public policy and liability reasons, lawyers must maintain in sacrosanct form the financial records of client and third party (including escrow) funds that come into their possession. While lawyers can choose to ignore their personal checking accounts to a "fare thee well", handling someone else's money imposes an affirmative and actionable duty to adhere to mandated rules. Indeed, if Massachusetts were to adopt a rule, such as the one in New Jersey, permitting random audits of IOLTA accounts, without prior notice to Bar Counsel of a dishonored check or a grievance having been filed, the ranks of practicing lawyers might be substantially thinner. See, for example, the Random Audit Program that has operated since 1981 under ***New Jersey Court Rule 1:21-6*** and ***Rule of Professional Conduct 1.15***.

Funds At Issue:

"Trust property" means property of clients or third persons that is in a lawyer's possession in connection with a representation and includes property held in any fiduciary capacity in connection with a representation, whether as trustee, agent, escrow agent, guardian, executor, or otherwise. Trust property does not include documents or other property received by a lawyer as investigatory material or potential evidence.

The Information Lawyers Must Maintain:

Rule of Professional Conduct 1.15(f)(1)(A) requires lawyers to record:

- the name and address of the bank or other depository
- the account number
- the account title
- the opening and closing dates of each account
- the type of account (whether it is an IOLTA account or a separate client fund account for the client).

For each account, there are three types of accounting records that must be kept by the lawyer. They are the following:

- a ledger for each client matter
- a ledger for bank fees and charges, and
- a check register.

A Ledger for Each Client Matter:

Rule 1.15 (f)(1)(C) requires attorneys to keep individual client records (or ledgers) for each separate matter in which the lawyer holds funds for a client. Each ledger

- must identify the name of the client
- detail all money received and paid out on behalf of the client or third party, and
- show the client's balance following every receipt or payment.

Every receipt and payment of money for a client must be recorded in the ledger for that client matter.

- For every receipt, list the date, amount and source of the money
- For every payment, list the date, the amount, the check number, the payee and the purpose of the payment
- After each receipt or payment is recorded, the new balance held for the client must be recorded.

A "Law Firm" Ledger for Bank Fees and Charges:.

Rule 1.15 (f)(1)(D) requires lawyers to record every bank charge against the client trust fund account in the corresponding check register and permits the lawyer to keep his or her money in the account to pay these charges and fees. Therefore, create a separate ledger of the firm's funds, label it as such, and use it in the firm management system to record every deposit of the lawyer's funds, every charge the bank makes against the account, and the running balance in both the client ledger and the check register.

Check Register:

Lawyers must have a separate check register for each account. There are no exceptions! Rule 1.15 (f) (1) (B) requires that a check register

- be in chronological order
- show the date and amount of all deposits
- contain the date, check or transaction number, amount and payee of all disbursements whether by check, electronic transfer, or other means
- show the date and amount of every credit or debit, and
- and identify the client matter and the current balance in the account.

The So-Called "Three-way" Reconciliation:

A three-way reconciliation under Rule 1.15 (f)(1)(E) requires the lawyer to add all of the individual client ledgers and the firm's ledger for bank charges and compare the total of the ledgers to the balance in the check register. Both amounts should be the same. If they are not, the basic records – the bank statements, the client ledgers, the bank charges ledger and the check register – need to be checked for mistakes and corrected.

When both amounts are the same, the lawyer should reconcile this amount against the bank statement in the usual manner of balancing any checkbook. The Rule requires that client trust account records be reconciled at least every 60 days and that the attorney maintain a written record that shows the records were reconciled be kept.

We suggest monthly reconciliations to make sure that wires actually made it into the correct account, that funds held back or intended to be held in escrow are removed from the IOLTA account and put into separate accounts for the benefit of the parties, and that title insurance, discharge and recording checks can be tracked and do not linger for months or years without being negotiated or, worse, without being deducted, thereby leaving artificially inflated balances.

Keep A Copy Of The Reconciliation Reports:

Lawyers must keep a copy of the reconciliation reports of the client ledgers, bank charges ledger, check register and bank statements. It is not optional. An attorney will be required to produce those records to Bar Counsel if a grievance is ever filed.

While all of this may seem like a lot of work, it is essential for a practice that is smooth and in compliance.

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