

GARDEN STATE CLE LESSON PLAN

A 1.0 credit course

**FREE DOWNLOAD
LESSON PLAN AND EVALUATION**

SURVIVING A DEMAND AUDIT

With

**Robert Ramsey
Garden State CLE Senior Instructor**

And

**Lee A. Gronikowski
Attorney & Lt. Col. (ret.)**

Program description

As a solo practitioner you have a wide range of responsibilities, not to mention your court appearances. As a result sometimes mistakes may be made. Learn how to avoid the deadly demand audit with this 1.0 ethics credit CLE.

I. Introduction

- **Lee Gronikowski – retired from Office of Attorney Ethics (19 years of service), now representing attorneys who are charged with ethics violations**
- **Demand audit – serious issue for NJ attorneys**
- **3 kinds of audits:**
 - **Random audit: every attorney subject to, selected at random based on your telephone number, AOC chooses the selectees, receive letter that want to look at trust and business accounts, not necessarily to find problems – to check compliance with R. 1:21-6 (Recordkeeping; Sharing of Fees; Examination of Records) – educational component as well, try to get attorney to understand how to maintain books and records, if there is a problem then no discipline case filed just ask attorney to certify within 45 days if problem is corrected; may suggest a class for attorney to learn the right way without a disciplinary record; rare for random auditor not to find something**
 - **Select audit: reserved for attorneys who had transgressed in the past and OAE decides to go in and verify compliance is still in place; target of investigation because of prior issues that were found; usually every year to 2 years depending on violation; typically violation is negligent or reckless record keeping function; rarest type of audit; only record keeping cases are subject to select audit; 10% of all audits; done at attorney's office with notice to the attorney; focus on trust account and will look at business account**
 - **Demand audit:**

II. Procedure leading to a demand audit

- **Grievance comes in that alleges misuse of funds**
 - **Early breaking of escrow – release of escrow without permission of other party (In re Hollendonner, 102 NJ 21 (1985)).**
 - **Susser case – used money for benefit of the client, still financial obligation, not a Wilson violation**
 - **Taking real estate deposits early – attorney borrows \$\$ from escrow account for business account, and then has to**

- repay the \$\$ back before closing; OR, a new deposit comes in and that covers the \$\$ previously borrowed (“lapping”)**
- **Many ways to learn of these violations**
 - **People who did not get settlements on time because mortgages not paid off after closing**
 - **Chancery Judges that escrow has been broken**
 - **Title companies who say this loan closed and mortgage not paid off**
- **Bounced checks out of trust accounts trigger issues – but not a demand audit**
 - **NJ banks have contract with Supreme Court – every time overdraft must be reported to OAE**
 - **Overdraft, line of credit and ATM cards connected to trust account are strictly forbidden**
 - **Trust accounts are under the microscope**
 - **If bounced check, bank sends letter to OAE; OAE asks attorney by letter for explanation – usually book keeping mistake**
 - **Counsel clients to send letter to OAE to explain why bounced checks – self reporting is best as opposed to OAE getting around to scrutinizing it – OAE won’t seem suspicious – resolved on paper and through the mail**
 - **Relatively common place for audit in this type of situation – OAE wants explanation to be 100% clear – so may send out auditor**
 - **Also depends on amount of money involved**
- **Hard to avoid demand audit if someone files grievance against you based on money**
- **Common for OAE to send a letter to attorney that says “show us your records or show us your license”**
 - **Give attorney 2 weeks – rare adjournments**
- **Deputy Ethics Counsel and member of audit staff will go to attorney’s office**
 - **Try to reconcile attorney trust account – where is money? How was it used?**
 - **Business account is a “passing interest” – unless there is trust money going into that account**
- **Demand audit – they are looking for trouble**
- **Most audit staff people have forensic accounting backgrounds**
- **Difficult to have someone temporarily suspended**

- **Supreme Court gives must leeway for attorneys to provide information to OAE for audit**
- **Proctorship**
- **Applications for temporary suspension are always done by OAE**
- **Supreme Court is extremely indulgent as long as you have an excuse to provide information in a short period of time**
- **After temporary suspension, ultimate resolution could be years away – so best to resolve the issue asap because you could have a temporary suspension longer the usual period of discipline (R.1:20-20 future activities of attorney who has been disciplined or transferred to disability-inactive status)**
- **No further investigation after complaint is signed for discipline**

III. The Demand Audit Date – what to expect, what to bring

- **If OAE is not making application for temporary suspension because person has been compliant and date is set for demand audit**
- **Show up with counsel**
- **Show up with an accountant if you have one or hire a forensic accountant**
- **Bring all attorney books and records**
 - **Bring bank statements**
 - **Business account**
 - **Checkbook**
 - **Business disbursements journal**
 - **Business receipts journal**
 - **Trust account**
 - **Trust checkbook**
 - **Trust disbursements journal**
 - **Trust receipts journal**
 - **Copies of all client ledger cards**
- **At audit – OAE will try to do a reconciliation for starters**
- **Almost every attorney who comes to demand audit does not have all these items**
- **OAE is specific about time period that they want to cover and look at – usually a 2 year period**
- **Hire forensic accountant or use CPA and make sure that reconciliation has been done before going to OAE so that when auditor does their job the numbers are adding up**

- **Show that you have been doing what you are supposed to be doing**
- **Many attorneys find book keeping the most onerous – simple ignorance makes things difficult for them**
- **This is not a criminal investigation – client should NOT be minimally cooperative**
- **Defense counsel has little to contribute that is helpful during an audit – client should answer not counsel**
- **Role of defense attorney is before hand –**
 - **making sure client has all paperwork,**
 - **everything is in balance,**
 - **explanations for what is out of balance,**
 - **suggestions for future to avoid problems in the future,**
 - **don't volunteer information to auditor but don't lie,**
 - **affirmative obligation to disclose an anomaly to auditor**
- **Without counsel, attorneys show up unprepared – attorneys are not good businessmen and therefore don't take care of paperwork**
- **Many software programs that can easily take care of book keeping**
- **TAME – Trust Accounting Made Easy – software program**
- **The demand audit is serious – career is in balance**
- **Bad situation can become worse if not cooperating with system or trying to hide things**
- **Possible outcome for lack of cooperation could be temporary suspension – months or years of suspension before resolution**
 - **Not always a “time served” situation – you may likely be subject to additional suspension even if you were on temporary suspension for a period of time**
 - **Even self-imposed suspension is not in your favor – In re Farr, 115 NJ 231 (1989)(you cannot impose your own suspension).**
 - **To be suspended you must be under R. 1:20-20 – if not then it is not a suspension under the rule of court and being supervised by OAE**
- **Cooperation, honesty by target of investigation**
- **If you have information that by Court Rule or by RPC that the auditor must know about, then you must disclose, i.e. another trust account (can become the subject of the audit – OAE may make this decision) – if OAE does not find out they may find out later and then you are in more trouble**
- **Preparation – ready with all documents and in balance**

- **If negligent misappropriation of funds – attorney should immediately pay back trust account; done ahead of time, account for attorney’s money to reimburse, have explanation**

IV. Defense counsel’s obligation

- **Prepare your client**
- **Name Counsel Defense – the more recognizable the attorney representing the respondent, the easier the court goes on the client when determining suspension**
- **Role is not adversarial – more collaborative**
- **Good discovery vehicle – learn where OAE is going to go and what is their focus**
- **May be able to resolve case ahead of time, unless Wilson violation**
- **Negligent misappropriation, poor office management – easy to stipulate – resolution**
- **Counsel can speak with client outside of audit if necessary**
- **Counsel cannot interfere with the process and let auditors do their job**
- **R. 1:20-3(g) – must cooperate with attorney ethics investigation**
- **Counsel cannot interfere with ability of auditors to ask questions and get answers from target**

V. Possible Outcomes of Demand Audit

- **More often than not audit generates requests for additional information**
- **Ultimate end of process is a report – recommendation either dismissal or discipline**
- **OAE must decide if they will file a complaint or allow diversion**
 - **Diversion**
 - **similar to PTI;**
 - **admonition;**
 - **cannot have other discipline in last 5 years;**
 - **as long as no serious misconduct;**
 - **Agreement in lieu of discipline prepared by OAE;**
 - **Respondent admits line by line what he/she did;**
 - **Conditions – no restrictions in court rules for what conditions may be applied;**
 - **Classes**
 - **Training**
 - **Apology**

- **Counseling**
- **Almost any condition is ok as long as legal and appropriate**
- **Outcomes can be: nothing; possible diversion for minor issues; if not appropriate for diversion, work with OAE stipulation and level of discipline agreed to by everyone; Wilson violation – disbarment**
- **In re Wilson, 81 NJ 451 (1979)**
 - **Never been a case wherein knowing misappropriation is found that there has not been a disbarment**
 - **Decide whether you want to go through process with counsel fees or just be disbarred**
- **In re Wigenton, 210 NJ 95 (2012)**
 - **Case looked like a Wilson case**
 - **Supreme Court determined that it was not a Wilson case, it was negligent misappropriation**
 -
- **Line between negligent and reckless/knowning is more clear cut**
- **In re Gross, 202 NJ 39 (2010) – attorney received tip from a client and he told the secretary; partners are angry because never disclosed tip; case goes to trial and attorney is disbarred under In re Siegel, 133 NJ 162 (1993) – knowing misappropriation of partnership funds; DRB recommendation is disbarment; trial before Supreme Court – disciplinary order (no decision at all) finding not clear and convincing evidence of misappropriation, found other RPC violation and suspended for 3 months**

VI. Additional advice

- **Potential respondents**
 - **Make sure records are up to date**
 - **Book from OAE – can request from OAE, available on Garden State CLE website – read it! – give it to your accountant if you are facing an audit**
 - **Maintain records contemporaneously**
- **R. 1:21-6 Recordkeeping; sharing of fees; examination of records**
 - **“you must keep you records in accordance with generally accepted accounting principles”**
 - **Means that you need to keep a running balance in your checkbook – at the very least**

- **Generally accepted accounting principles is not defined by OAE – defined by the field of accounting**