

Garden State CLE presents:

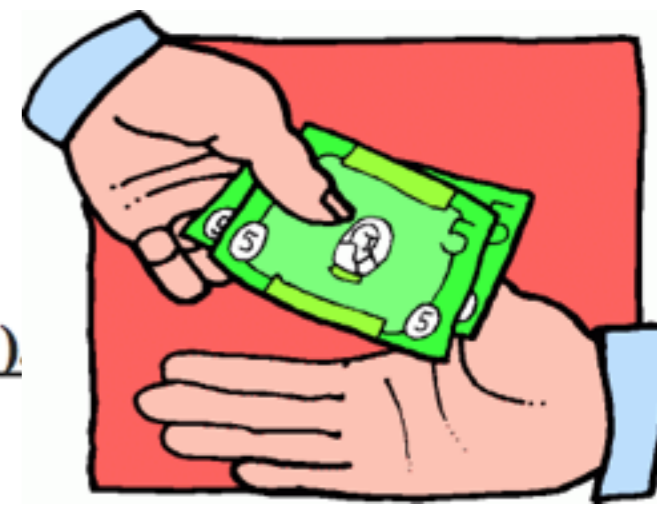
Trust Account Tune Up:

**Are your books record ready for a
surprise audit?**



Lesson Plan

Part I - Financial Obligations of New Jersey Attorneys - In general



a. "Knowing misappropriation" - In re Wilson, 81 NJ 451, 454 (1979)

Like many rules governing the behavior of lawyers, this one has its roots in the confidence and trust which clients place in their attorneys. Having sought his advice and relying on his expertise, the client entrusts the lawyer with the transaction including the handling of the client's funds. Whether it be a real estate closing, the establishment of a trust, the purchase of a business, the investment of funds, the receipt of proceeds of litigation, or any one of a multitude of other situations, it is commonplace that the work of lawyers involves possession of their clients' funds. That possession is sometimes expedient, occasionally simply customary, but usually essential. Whatever the need may be for the lawyer's handling of clients' money, the client permits it because he trusts the lawyer.

It is a trust built on centuries of honesty and faithfulness. Sometimes it is reinforced by personal knowledge of a particular lawyer's integrity or a firm's reputation. The underlying faith, however, is in the legal profession, the bar as an institution. No other explanation can account for clients' customary willingness to entrust their funds to relative strangers simply because they are lawyers.

Abuse of this trust has always been recognized as particularly reprehensible.

What are the merits in these cases? The attorney has stolen his clients' money. No clearer wrong suffered by a client at the hands of one he had every reason to trust can be imagined. The public is entitled, not as a matter of satisfying unjustifiable expectations, but as a simple matter of maintaining confidence, to know that never again will that person be a lawyer. That the moral quality of other forms of misbehavior by lawyers may be no less reprehensible than misappropriation is beside the point. Those often occur in a complex factual setting where the applicability or meaning of ethical standards is uncertain to the bench and bar, and especially to the public, which may not even recognize the wrong. There is nothing clearer to the public, however, than stealing a client's money and nothing worse. Nor is there anything that affects public confidence more much more than the offense itself than this Court's treatment of such offenses. Arguments for lenient discipline overlook this effect as well as the overriding importance of maintaining that confidence.



In summary: maintenance of public confidence in this Court and in the bar as a whole requires the strictest discipline in misappropriation cases. That confidence is so important that mitigating factors will rarely override the requirement of disbarment. If public confidence is destroyed, the bench and bar will be crippled institutions. Functioning properly, however, in the best traditions of each and with full public confidence, they are the very institutions most likely to develop required reform in the public interest.

b.) Disciplinary process:

Normally, the disciplinary process involves a review of the facts, a consideration of aggravating and mitigating factors, a comparison to past similar disciplinary cases and a fair measure of discipline that will protect the public and deter future acts of misconduct.

In *Wilson* cases, once the underlying knowing misappropriation of client funds can be proven by clear and convincing evidence, no other analysis is undertaken. The only remaining step is the imposition of discipline in the form of disbarment.

c. "Negligent or reckless" - In re Noonan, 102 NJ 157 (1986): In re Konopka, 126 NJ 225 (1991).

The rule set forth in *Wilson* is aimed at attorneys who have knowingly misappropriated client funds. Essentially, the attorney must know that the funds belong to a client, knowingly take the funds, and do so without the client's consent. Negligent or sloppy bookkeeping, mistakes and reckless misappropriation will all result in some form of discipline, but does not trigger "almost invariable" disbarment.



d. Expansion of the *Wilson* Rule to other recordkeeping responsibilities:

In re Hollendonner, 102 NJ 21 (1985) - Escrow funds

In re Siegel, 133 NJ 162 (1993) - Law firm fees and expenses

In re Greenberg, 155 NJ 138 (1998) - Law firm fees and expenses

But see In re Sigman, 220 NJ 141 (2014) (30 month suspension)

e.) Rules of Professional Responsibility

RPC 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 a financial institution in New Jersey. Funds of the lawyer that are reasonably sufficient to pay bank charges may, however, be deposited therein. 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 seven years after the event that they record.

f.) The Rules of Court

Rule 1:21-6(a). Recordkeeping; Sharing of Fees; Examination of Records (a) Required Trust and Business Accounts. Every attorney who practices in this state shall maintain in a financial institution in New Jersey, in the attorney's own name, or in the name of a partnership of attorneys, or in the name of the professional corporation of which the attorney is a member, or in the name of the attorney or partnership of attorneys by whom employed



Part II - The random audit program

a.) What is the Random Audit Program?

Since 1981, the New Jersey Supreme Court has operated a program for random audits of attorney trust and business account records to determine compliance with the Supreme Court of New Jersey's mandatory recordkeeping rule, [R.1:21-6](#), and ethics rule [RPC 1.15](#) ("Safekeeping Property"). The Random Audit Program is administered through the Supreme Court's Office of Attorney Ethics.

The Random Audit Compliance Program conducted a record 730 audits of law firms in 2016. Nine (9) lawyers were disciplined (including three disbarments) through the detection efforts of the Random Audit Compliance Program.



The central purpose of the New Jersey Random Audit Program is the education of New Jersey attorneys on the proper method of compliance with their recordkeeping and ethical responsibilities under [R.1:21-6](#) and [RPC 1.15](#).

A secondary purpose underlying random audits is deterrence. Just knowing that there is an active auditing program is an incentive, not only to keep good records, but also to avoid temptations to misuse trust funds.

Finally, there is the purpose of detection of misappropriation. Since the random selection process results, by definition, in selecting a representative cross-section of the Bar, a few audits inevitably uncover some lawyer misappropriation.



b.) How are Random Audits Conducted and how are Attorneys Selected to be audited?

An annual random selection of audit candidates is made from the statewide list of licensed attorneys using the law firm as the entity subject to audit, rather than individual attorneys. Every attorney in private practice is regarded as a member of a law firm. A law firm may consist of one or more attorneys, and the law firm identifier is the 10 digit "main" office telephone number. That number is captured for all private practice attorneys annually as part of the Attorney Registration Program.



Is the Selection Really Random?

The selection process is accomplished by a computer program that annually selects approximately 500 audit candidates using a tested random selection methods with is documented in its ability to produce truly random results. As a result, every law firm, regardless of size, has an equal chance of being selected for an audit.

How does the Audit Proceed?

Once an attorney or law firm is selected, the attorney or firm is provided with written notice 10 days to two weeks in advance of the scheduled date.

Generally, only one auditor is assigned to a matter. Occasionally, two or more auditors are assigned if a large firm or other complicating feature is involved.

It is preferable for the attorney to be present at the audit. If the attorney cannot be present, a responsible person knowledgeable about the books and records must be available.

On arriving at the law office, the auditor conducts an initial interview with the attorney or responsible person left in charge. Detailed information about the firm's recordkeeping procedures is secured and recorded on a Random Audit Questionnaire form. The auditor also conducts a review of the firm's trust and business account books and records in order to determine compliance with the rule requirements. The review culminates in a reconciliation of the attorney's trust account (or accounts) as of the date of the most recent bank statement.

Any recordkeeping deficiencies are noted by the auditor on a Recordkeeping Deficiencies Checklist which contains a brief description of the most commonly found recordkeeping deficiencies. The auditor provides a copy of the checklist to the attorney or person left in charge, and, in an exit conference, discusses with that individual the corrective actions that should be taken to remedy any deficiencies which have been found.



Shortly after the audit, the attorney is formally advised by correspondence of the results. If the audit revealed no problems, a closing letter is forwarded that acts as the final disposition of the matter. If minor deficiencies were discovered, a deficiency letter is sent to the attorney describing the shortcomings that require corrective action. The source of information for the deficiencies is the aforementioned Recordkeeping Deficiencies Checklist.

What happens if there are Minor Deficiencies?

Within 45 days after the date of the deficiency letter, the attorney is required to submit a response addressing the corrective action taken for the cited recordkeeping deficiencies. On receipt of an acceptable response from the attorney, the matter is closed. If the attorney does not respond, the matter may be referred to the Office of Attorney Ethics for disciplinary action.

What happens if there are Major Deficiencies?

If, at any point during the audit process, major deficiencies are discovered, such as misappropriation of client's trust funds, the matter is referred immediately to the Office of Attorney Ethics for disciplinary action. Historically, such referrals are made in less than 1% of the audits conducted.



DISCIPLINARY QUESTIONNAIRE



I. GENERAL INFORMATION:

1. Admission Information – Jurisdictions/Year Admitted

(Check all applicable jurisdictions and state year of admission)

- New Jersey _____
- Pennsylvania _____
- New York _____
- _____
- Any other jurisdiction(s) w/year admitted _____

2. Practice Information

Describe main area of practice (solo/firm/partnership) and list areas of practice during audit period.



II. ACCOUNTING INFORMATION

1. Have you ever taken an accounting class?
2. Have you ever taken the Skills & Methods course?

(if admitted after 1987 attorney had trust & business accounting)

3. Have you (office/firm) ever been the subject of a random audit?

If yes, when? _____

4. Are you familiar with NJ Recordkeeping rule 1:21-6?
5. Did you have an accountant during audit period?

Accountant's name, address & telephone number:

Dates employed:



Description of Responsibilities:

Was the accountant made aware of R.21-6 requirements?

6. Did you employ a bookkeeper during the audit period?

Bookkeeper's name, address & telephone number:

Dates employed:

Description of Responsibilities:

Was the bookkeeper made aware of R.21-6 requirements?

7. If neither an accountant nor a bookkeeper was employed, who was responsible for your trust and business accounts during the audit period?



8. ATTORNEY ACCOUNTS

a. Primary Attorney **Trust** Account

BANK:

Account Designation:

Account #:

Date Opened:

Date Closed:

Is there a master account with subaccounts for individual clients?

Authorized Signatory(ies) during audit period:

Is a signature stamp ever used for trust account checks?

Check box of all records maintained for the trust account during the audit period and identify who prepared those records:

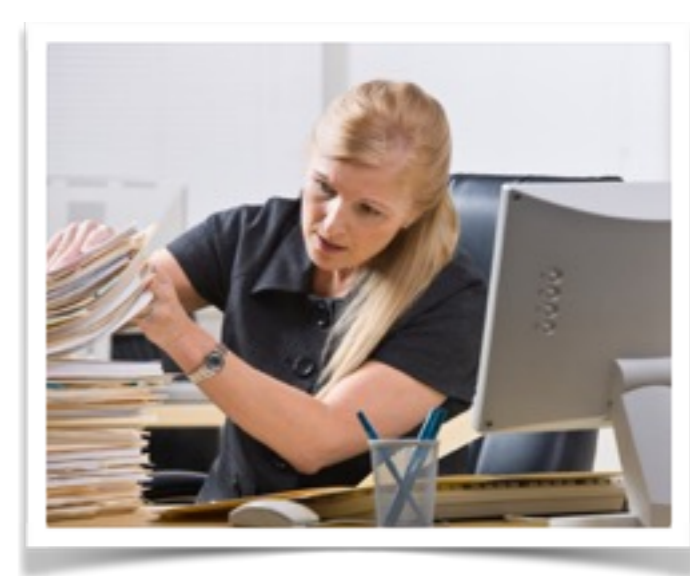


- checkbook
- client ledger sheets
- checks (original/digital)
- monthly reconciliations
- receipts journal
- disbursements journal
- deposit slips (original/digital)

Prepared by:

Indicate in what format(s) the records are maintained:

- | | |
|--------------------------------------|---|
| <input type="checkbox"/> manual | <input type="checkbox"/> computerized (software?) |
| <input type="checkbox"/> one-write | <input type="checkbox"/> accu-track |
| <input type="checkbox"/> other _____ | |



b. Primary Attorney Business Account

BANK:

Account Designation:

Account #:

Date Opened:

Date Closed:

Is there a master account with subaccounts for individual clients?

Authorized Signatory(ies) during audit period:

Check box of all records maintained for the trust account during the audit period and identify who prepared those records:



- checkbook
- disbursements journal
- deposit slips (original/digital)
- receipts journal
- checks (original/digital)

- any ATM
 - any cash w/d
 +/a

Prepared by:

Indicate in what format(s) the records are maintained:

- manual
- computerized (software?)
- one-write
- accu-track
- other _____



Deposit

date _____ your name _____

Name _____

Account Number _____

The Money Bank
 Cashton, NC 22222

CASH		
CHECKS		
Subtotal		
Less Cash		
TOTAL		

list the amount of each item that you are depositing here

sum of all the items deposited

amount of cash you want back

your account number

total amount of deposit

9. ACCOUNTING PRACTICES

Describe your office procedure for handling trust funds in general, providing names and titles of those involved.

- a) Preparing and signing checks
- b) Preparing and making deposits (including electronic transfers)
- c) Reviewing monthly bank statements
- d) Preparing monthly reconciliations

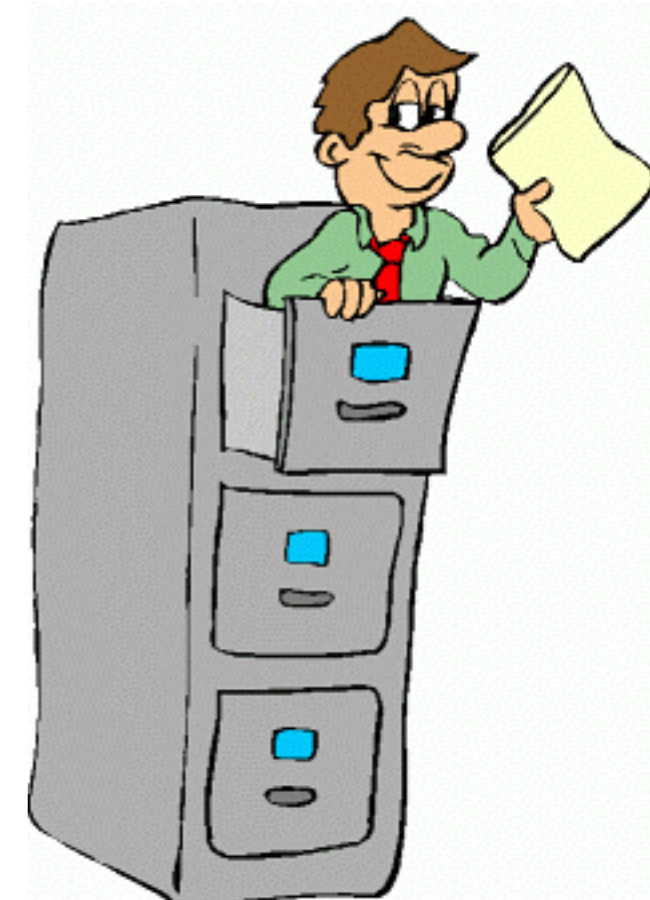


10) List any other accounts maintained during the audit period, whether in New Jersey or elsewhere – including other trust or business accounts, payroll accounts, cost accounts, estate accounts, receiverships, guardianship accounts,

conservatorships, any other fiduciary accounts, dormant accounts or accounts that were closed during this time. All accounts for which you are an authorized signatory should be included. Be specific as to the type of account, dates opened/closed, what records are maintained for each account, the format of those records, whether monthly reconciliations are prepared and who prepares the reconciliations. (Attach a separate sheet if necessary.)

Type of Account:

Bank:



Account Designation:

Account #:

Date Opened:

Date Closed:

Authorized Signatory(ies) during audit period:

Type of Account:



Bank:

Account Designation:

Account #:

Date Opened:

Date Closed:



22) Did you have signatory authority over any other fiduciary accounts during the audit period?

If yes, please list.



23) Do you have Power of Attorney for anyone, clients or non-clients?

If yes, please list.

24) Have you ever borrowed trust funds or other monies from a client?

If yes, identify the client(s), explain the circumstances, provide the date of the loan(s) and answer the following questions:

Client(s): _____

- a) **Were formal loan agreement prepared?**
 - b) **Was the client advised to seek independent counsel?**
 - c) **Did the client consent in writing to the loan transaction?**
 - d) **Is there borrowed money from any client that has not yet been repaid?**
- 25) **Did you ever loan money to a client?**



elective

appointed

local

county

state

federal

Please list the title held and dates of service. _____

6) Are you incorporated or do you operate as a PC or LLP?

7) Do you carry malpractice insurance? If so, what are the policy limits?

8) Do you meet current CLE requirements?

9) Have you ever been sued for malpractice?

10) Have you ever been the subject of an ethics grievance; if so, what was the result?



Authorized Signatory(ies) during audit period:

Type of Account:

Bank:

Account Designation:

Account #:

Date Opened:

Date Closed:

Authorized Signatory(ies) during audit period:



11) Have client funds, including cash, ever been deposited in an account other than an attorney trust account or kept elsewhere?

If yes, explain.

12) Have you deposited non-client funds in a trust account other than personal funds for bank charges?

If yes, explain.

13) Have you ever transferred funds from the trust account electronically?

If yes, explain.

- Are there written transfer instructions signed by you (if not, who signed?)
 - Written confirmation from bank with date, payee and amount?
- 14) Do you have an ATM card for the trust account(s)?
- 15) Are there any CASH withdrawals from the trust account(s)?
- If yes, explain/identify:
- 16) Do you have overdraft protection for the trust account(s)?
- 17) Do you maintain your bank records and client files for 7 years?

18) Were there any unidentified/unclaimed funds held in the trust account(s) during the audit period?

If yes, explain how long funds have been in the account; the amount; if possible, identify the client and state any and all efforts to identify/disburse the funds.

19) Are legal fees withdrawn from trust promptly when earned?

20) Are all legal fees deposited to a business/office/professional account?

21) Are you an administrator, executor guardian or trustee?

If yes, please list.



If yes, identify the client(s), explain the circumstances and state whether there is any written documentation regarding the loan and whether the loan has been repaid.

26) Have you ever engaged in a business transaction with a client(s)?

If yes, identify the client(s), explain the transaction and state whether there is any written documentation regarding the transaction.

Was client(s) advised to seek independent counsel?

27) Were any of the records produced for this audit prepared for you after you received the audit notice?

If yes, please identify what records were prepared for the audit, when the records were prepared and by whom.



III. MISCELLANEOUS

- 1) Have you ever filed for bankruptcy?**
- 2) Has the firm ever filed for bankruptcy?**
- 3) Are you holding any valuables, other than money, for clients?**

If yes, identify what is being held and where.

- 4) Do you collect any mortgages or other investments for clients?**

If yes, identify what you collect, the amount and where the funds are deposited.

- 5) Do you hold any public offices? (If yes, check appropriate boxes.)**

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