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MORE DISHONORED IN THE BREACH: Bounced Checks and Bad Bookkeeping

by
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With apologies to Hamlet, Shakespeare is so popular these days that perhaps wordplay is the thing wherein we'll catch the attention of the Bar, if not the conscience of the king, even on the subject of dishonored checks and financial records.

Almost four years after the implementation of the dishonored check rule (Mass. R. Prof. C. 1.15(f) and its predecessor DR 9-103), notices from financial institutions of dishonored checks drawn on trust accounts, and files opened as a result of our receipt of those notices, continue to arrive at the Office of Bar Counsel at a rate of about 300 a year. Net of those subsequently expunged because of bank error, there were 260 total in 1998 and 87 already in the first three months of 1999.

Putting aside the rarer instances of more serious discipline that have their genesis in notices of dishonored checks (including a recent indefinite suspension), 13 (private) admonitions in 1997, 15 admonitions in 1998, and three admonitions to date in 1999, began with dishonored check notices. And while not as numerous as the dishonored check cases, other admonitions during these years also arose from problems with trust accounts. These latter come to Bar Counsel's attention from a variety of sources-- often disgruntled clients or beneficiaries, but sometimes lawyers' attempts to pay their annual registration fees to the BBO with trust account checks!

In all of the admonitions, the misconduct is not intentional. The disciplinary action generally has its root in the lawyer's failure to maintain adequate trust account records or in a bookkeeping system that is otherwise improper in one or more respects. Sometimes the lawyer is commingling by depositing earned fees (that is, fees already earned when paid, as opposed to retainers, which are fees paid in advance) or other personal or business funds to a trust account. Occasionally, an operating account is incorrectly labeled as a trust account. Very often, no individual clients ledgers are maintained so that the lawyer has no straightforward method of zeroing out receipts and disbursements for specific clients. And very commonly, the account is not routinely reconciled, or is not adequately reconciled, either internally or to the bank statements on a monthly, or even quarterly, basis. Among other problems, the lawyer therefore does not know what checks remain outstanding or has not accounted for wire fees or check charges or other service charges.

However, the remainder of this article will concentrate on one of the most frequent—and most easily preventable—causes of bounced checks. Bar Counsel's investigation shows that, in many instances, lawyers are not withdrawing fees from their trust accounts as earned, but instead are paying themselves fees piecemeal, as needed. The deficiency occurs when the lawyers eventually lose track of what earned fees remain in the account, overpay themselves, and end up short the funds needed to cover another check. In at least five of the 1997 admonitions, six of the 1998 admonitions, and all three of the 1999 admonitions to date, this precise issue was one of the attorney's principal problems.

Mass. R. Prof. C. 1.15(d)(2), like its predecessor DR 9-102(B)(2), requires that fees due must be withdrawn from the trust account at the earliest reasonable time after the lawyer or law firm's interest becomes fixed. Failure to do so in and of itself constitutes commingling. That is, even if the lawyer keeps an accurate record of fee withdrawals and no checks are dishonored, leaving earned fees in a trust account is improper.

When checks do bounce in these circumstances, however, the underlying facts are often fairly predictable. A typical scenario goes something like this. A lawyer is entitled to a contingent fee of $5000 from a $15,000 personal injury settlement. Once the deposit of the settlement check to the IOLTA account clears, the lawyer immediately and properly pays out $10,000 to or for the client. However, instead of writing a check for her $5000 fee, the attorney writes herself a check for only $2000, the amount that she needs at the moment for office or personal expenses, and leaves the $3000 balance in the IOLTA account. Over the next several weeks or months, the lawyer withdraws walking-around money from the account for herself in increments of $100 or $200 or $500, all of which she mentally attributes to the balance of this personal injury fee. Perhaps she also compounds the commingling by paying office expenses such as postage, or personal expenses such as a car payment, directly from the trust account with the funds she believes she is still due in fees.

Then, making a bad practice worse, the lawyer does not keep a running tally. Eventually she pays herself a total of $5400, rather than $5000. The account is now $400 short. Often, this same practice is ongoing with multiple settlements simultaneously. The lawyer may end up estimating amounts still due her and withdrawing fees in round amounts without particular reference to any one case. Frequently, lawyers in these circumstances also do not take note of outstanding checks that have not been negotiated and simply assume that any sum remaining in the account is the balance due the lawyer for fees. Inevitably, at a point when the account balance is low and there is no float to cover the shortfall, an unrelated check will bounce.

The same problem can occur with retainers. A lawyer may have been paid a retainer of $2500 in a divorce. He properly deposits this sum to a trust account. What is supposed to happen is that, as work is done, the attorney sends a bill to the client, gives the client the opportunity to raise objections, and then withdraws the full amount of the bill from the trust account. Instead, in problem cases, we may find that the lawyer is making partial payments to himself from the retainer as the case goes along, but without necessarily having billed the client and without keeping track of the total of the withdrawals. Again, the lawyer ends up inadvertently overpaying himself and again the problem may be compounded if several retainers (or a combination of retainers and fees from settlements) are being expended in this manner at the same time.

The very simple solution to this problem is to follow the dictates of Mass. R. Prof. C. 1.15(d)(2). If a fee is withdrawn in full "at the earliest reasonable time after the lawyer's or law firm's interest...becomes fixed," these types of errors cannot occur. When a contingent fee case is settled (and assuming no dispute over fees with the client), the entire contingent fee should be withdrawn from the trust account after the settlement check clears. Fees due from settlements in noncontingent cases should be billed and withdrawn in full if there is no dispute. Similarly, the client should be billed before any portion of a retainer is withdrawn and then (and again assuming no dispute) the full amount of the bill should be removed from the account.

One final thought. For many of the same reasons, it is also dangerous to pay yourself fees from two or more cases in one combined check. In theory, good record keeping should enable you to split the payment and properly attribute it among several matters. In practice, this is another easy way to make errors that do not get detected until too late.