

Is Missouri's Trust Account Overdraft Notification Rule Working?

By Nancy L. Ripperger

What is the Trust Account Overdraft Notification Rule?

On October 8, 2009, Missouri became the 40th state to adopt a trust account overdraft notification rule.¹ The rule went into effect on January 1, 2010.

The rule and the regulation implementing it are very simple. The rule provides that every lawyer practicing or admitted in Missouri is deemed to have consented to overdraft reporting by any financial institution holding a client trust account. Rule 4-1.15(g).

The Missouri Advisory Committee, as directed by Rule 4-1.15(g), promulgated a regulation implementing Rule 4-1.15(g). The regulation requires financial institutions to agree to report to the Chief Disciplinary Counsel ("CDC") *any time* a check or debit is presented against the lawyer's trust account if the account contains insufficient funds to pay the item. This includes making a report to the CDC even when the financial institution returns the item unpaid.

What is the Purpose of the Rule?

The overdraft notification rule has several purposes. Its primary purpose is to serve as an early warning

system to the CDC when an attorney violates Rule 4-1.15² so that the CDC can intervene when the problem first occurs.³ This is particularly important when the violation involves misappropriation of client/third party funds. The rule is also designed to have a deterrent effect on attorneys who might contemplate misappropriating client funds or engaging in sloppy trust accounting practices and procedures.⁴ The thought is that an attorney who knows his trust account activities are being monitored will be more careful and trustworthy regarding trust account activities. Finally, it helps disciplinary authorities in identifying attorneys who need trust account training.

What Were the CDC's Initial Expectations Regarding the Overdraft Notification Rule?

Based upon the initial number of overdraft notifications received in January 2010 and the experience of other states, the CDC anticipated receiving approximately 300 overdraft notification notices in 2010. The CDC projected the number of overdraft notices would decrease in the following years as attorneys became more aware of the rule and the CDC offered more training and education to attorneys.⁵

The CDC predicted most overdrafts

would occur because of lack of adequate practices and procedures upon the part of the attorney. These poor practices and procedures would include: (a) failing to reconcile the trust account on a regular basis, resulting in errors going undetected; (b) disbursing settlement funds before the deposited settlement funds were available for withdrawal; (c) failing to keep adequate funds in the account to cover service charges; and (d) commingling client and attorney funds without adequate records as to the source of the funds.

Instead of disciplining all attorneys who overdrew their trust accounts, the CDC anticipated cautioning most attorneys and then providing training and resources for the attorney to improve his or her trust account practices. Of course, the CDC expected that there would be a small number of cases in which the attorney had engaged in fraudulent or dishonest activities or engaged in a serious pattern and practice of violating Rule 4-1.15. The CDC anticipated seeking formal discipline in these instances.

What Did the 2010 Statistics Show?

Most of the CDC's predictions were "right on the money," pardon the pun. In 2010, the CDC opened 280 overdraft investigations. Some of the investigations included multiple overdraft notices on the same account.

Thus, the number of notices the CDC actually received equaled or exceeded the 300 originally predicted.

The CDC's staff has completed 276 of these investigations. Of the completed investigations, the CDC: (a) closed 73 investigations without disciplining or cautioning the attorney; (b) closed 156 investigations by cautioning the attorney to improve his or her practices, (c) issued 29 admonitions to attorneys; (d) entered into two diversion agreements with attorneys, and (e) determined that 16 investigations warranted the filing of formal charges against the attorney.⁶

Of the 73 investigations closed without discipline or caution, a large majority were closed because of bank error. These included mistakes by the bank of imposing a service charge to a trust account when the account should have had no charge, posting a check to the wrong account, etc. Two cases were closed because the attorney died during the investigation and five additional cases were closed because the attorney was suspended or disbarred on other disciplinary charges while the overdraft investigation was pending.

In 2010, 56 overdrafts occurred because of accounting errors such as simple addition or subtraction errors in the check ledger or failing to keep accurate, up-to-date records. Fifty-two of the 56 were closed or closed with caution because the attorney generally had good accounting practices in place and the overdraft resulted from simple error or a temporary lapse in practices and procedures. Four attorneys received admonitions. The attorneys receiving the admonitions had other issues with their trust account or had already received some remedial assistance from the CDC and had failed to heed the advice given.

Thirty-three of the overdrafts

resulted from the attorney's failure to reconcile the trust account. Twenty-six of these cases were closed or closed with caution, two attorneys entered into diversion agreements with the CDC, and five attorneys received admonitions for failing to reconcile their accounts. The attorneys receiving cautions had procedures in place to reconcile their trust accounts but failed to follow the procedures every month. The attorneys receiving admonitions or entering into a diversion agreement did not regularly reconcile their trust accounts.

Sixty-six overdrafts occurred when an attorney drew upon deposited funds before the funds were available for withdrawal. This most frequently occurred when an attorney provided clients with settlement proceeds at the same time or before the attorney had deposited the settlement check into his or her bank account. Fifty-four of these attorneys were cautioned and nine received admonitions.

Of the 16 cases in which the CDC found that it was necessary to file formal charges, the Supreme Court has issued discipline in five of the cases. Two attorneys received public reprimands and two attorneys were disbarred after defaulting. Both of the disbarments involved misappropriations, one in which the misappropriation exceeded \$200,000. The CDC also obtained one interim suspension of an attorney's license based upon an overdraft notice. This case involved misappropriation and forgery.

The other 11 cases in which information has been or will be filed involve misappropriation or commingling of funds, and at least two of the cases involve attorneys lying to CDC staff.

What Has Happened in the First Six Months of 2011?

As of June 30, 2011, the CDC has opened 107 overdraft investigations. CDC staff has completed its investigation in 86 of these cases. Of the 86 investigations completed, the CDC: (a) closed 20 primarily because of bank error; (b) cautioned 56 attorneys primarily due to accounting/math errors on the part of the attorney or premature disbursement of settlement funds; (c) issued eight admonitions to attorneys primarily because of accounting errors; and (d) is preparing charging documents on two other cases because of serious commingling or misappropriation of funds.

Is the Overdraft Notice Rule Serving Its Purpose?

The overdraft notice rule is serving its purpose very well. It has fulfilled its primary purpose of alerting the CDC of misappropriation at an early stage, while losses can be minimized. Because of the rule, the CDC has identified seven attorneys who were misappropriating funds from their trust account and five of these attorneys have already been suspended or disbarred from the practice of law. One of these attorneys had no prior disciplinary history and one attorney only had two prior admonitions unrelated to the attorney's trust account. Without the trust account overdraft, the misappropriation could have gone on for a very long time and additional clients could have been harmed.

The number of overdraft investigations initiated in 2011 is down about 27 percent from last year⁷ and there also appears to be a decrease in the number of serious

violations discovered. Thus, the rule seems to be serving its second purpose of encouraging attorneys to be more careful regarding their trust account practices and to deter attorneys from stealing from their trust accounts. Although the numbers are going down, there is still vast room for improvement when you compare Missouri's figures with those of other states with a comparable number of attorneys. For example, in 2009 the Minnesota⁸ Lawyer Responsibility Board only received 81 overdraft notices for the whole year, with only three of the notices resulting in formal discipline.⁹ Missouri has already opened 107 investigations in the first six months of 2011.

Finally, the rule has provided a way for the CDC to identify attorneys who need additional training in trust accounting practices. The CDC urged each attorney who received a caution letter or admonition to review The Missouri Bar's Trust Accounting Handbook¹⁰ and to obtain trust account training via various CLEs. To ensure that appropriate training classes were available, in 2010 the CDC conducted four trust accounting seminars in various locations throughout the state and then provided four online webinars. The seminars and online webinars were very inexpensive to attend.¹¹ Unfortunately, many of the attorneys needing the training did

not participate. Of the more than 150 attorneys urged to obtain trust accounting training, only 60 obtained the training. Also of concern to the CDC is the fact that 14 different attorneys have overdrawn their trust account more than one time since the rule went into effect, with two attorneys overdrawing their trust account three or more times. While the CDC has chosen to caution many attorneys for more minor trust account violations, the CDC will begin pursuing discipline against attorneys who have chosen to ignore the warnings given and the training offered by the CDC.

Endnotes

1 The following jurisdictions have a trust account overdraft notification rule: Alabama, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Hawaii, Idaho, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Montana, Nebraska, Nevada, New Jersey, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Utah, Vermont, Virginia, Washington and Wisconsin. Michigan became the 41st state to adopt the rule. Its rule went into effect on September 15, 2010, after Missouri's rule.

The following jurisdictions do not have a trust account overdraft notification rule: Alaska, Illinois, Mississippi, New Hampshire, New Mexico, South Dakota, Texas, West Virginia and Wyoming.

Information obtained from the ABA Standing Committee on Client Protection.

2 Missouri's attorney trust account rule is found in Supreme Court Rule 4-1.15.

3 Lynda C. Shely, *The ABA Model Rules For Trust Account Notification And Model Rule For Payee Notification: Client Protection For The Next Millennium*, 11 PROF. LAW 23 (Spring 2000).

4 Shely, *supra note 3*.

5 Both Montana and Minnesota have had a trust account overdraft notice rule in place for more than 15 years. In recent years, the number of overdrafts in these states has decreased significantly. James E. Aiken, *Trust Account Overdraft Notification Rule*, THE MONTANA LAWYER, August 2007; Betty Shaw, *Overdraft Notification*, 63 No. 4 BENCH & BAR OF MINNESOTA (April 2006).

6 When filing formal charges against an attorney, the CDC seeks a reprimand, suspension or disbarment of the attorney's license.

7 On June 30, 2010, the CDC had initiated 146 overdraft investigations. On June 30, 2011, the CDC had initiated 107 overdraft investigations. This is a decrease of 27 percent.

8 An ABA 2009 Client Security Fund Survey showed 25,749 attorneys admitted in Minnesota and 28,000 attorneys admitted in Missouri.

9 Martin Shaw, *Time is Money*, 67-Jul No. 4 BENCH & BAR OF MINNESOTA 14 (July 2010).

10 The Missouri Bar Lawyer Trust Account Handbook is available at <http://members.mobar.org/ssf2011-cm/materials/trust%20account%20handbook.pdf>.

11 The online webinars only cost \$35 and provided the attorney with 1.2 hours of ethics continuing education.



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