NEW YORK STATE BAR ASSOCIATION
ONE ELK STREET ALBANY, NEW YORK 12207 TEL. (518) 463-3200

Committee on Professional Ethics

Opinion 554 - 11/21/83 (22-83)

Topic: Interest on lawyer accounts.

Digest: Lawyers may participate in programs to provide financial support for legal services through deposit in a commingled interest-bearing account of client funds held for a short period of time or nominal in amount where such funds if not aggregated would not produce income.

Code: DR 9-102.

QUESTION

May a lawyer participate in a program established by state statute to provide financial assistance to civil legal services programs and for other purposes affecting the administration of justice through deposit in a commingled interest-bearing trust account of client funds held for a short period of time or nominal in amount?

OPINION

The New York State Bar Assocation's Special Committee to Study Alternative Sources of Funding for the New York Legal Services Council, having supported the enactment of legislation which would establish a non-mandatory program to provide financial support for legal services and other purposes through deposit by lawyers in an interest-bearing trust account ("IOLA program") of client funds held for a short period of time or nominal in amount, asks what would be the ethical obligations of an attorney who elects to participate in the IOLA program.

Over the past several years concern has mounted in the legal community as to how best to meet the need to provide civil legal assistance to the poor in the face of substantial cutbacks in federal funding of programs providing these services. In a number of states, programs have been proposed,

and in some cases implemented, to provide financial support for these programs and other similar public service projects from interest earned on lawyers' trust accounts in depository institutions. Ethical questions arise as to the propriety of depositing client funds in such a commingled trust account.

A basic tenet of general application with respect to the lawyer-client relationship is contained in DR 9-102, which requires that funds deposited in a lawyer's trust account, which by definition are the client's funds, be kept separate and apart from the lawyer's funds and that any interest earned on those funds belongs to the clients. N.Y. State 90 (1968); N.Y. City 81-68 (1982); N.Y. City 79-48 (1980). In most instances these funds are held by an attorney for a short period of time to be used for a specific purpose by the attorney on behalf of the client. Generally separate accounts are not established; rather, the funds are commingled with other client funds, but because suballocation of interest is neither practical nor cost-effective the funds are held in non-interest bearing accounts. However, if any interest is earned by these accounts or on any separate trust account maintained by a lawyer for the benefit of a client, that interest, absent the client's consent, belongs to the client. DR 9-102(B); N.Y. City 81-68 (1982).

Where a lawyer holds a sum for a client which is sufficient to earn interest, the lawyer has a fiduciary obligation to invest that sum, 2 Scott, Law of Trusts, Sections 180.3, 181 (3d ed. 1967), and an ethical obligation to notify the client of receipt of the funds, and any interest thereon, maintain adequate records and make prompt payment of both principal and interest. DR 9-102(B)(1), (3), (4).

The question remains whether this ethical analysis is applicable to interest earned on clients' funds, too nominal in amount or held for too short a period of time to generate interest in a separate account, but which when aggregated with other client funds may generate interest which by statute is to be paid to tax-exempt organizations for the support of legal services or other purposes defined by the legislature.

The question can be resolved by examining whether or not the income generated by the aggregated funds can be classified as clients' property. Since it is currently not economically feasible for financial institutions to suballocate these funds and provide clients with interest, it can be fairly said that the client does not have a reasonable expectation of receiving interest sufficient to support a claim of entitlement. Where other similar programs have been established the Internal Revenue Service has ruled that as long as the client has no right to determine whether the funds will be placed in the trust account the income generated is not taxable to the client. Thus, courts (see Matter of

Interest on Trust Accounts, 402 So. 2d 389 (Fla. 1981)), legislatures and other ethics committees (see ABA 348 (1982)) have concluded that the ethical constraints set forth in Canon 9 are not applicable to interest so generated.

Under the plan adopted by statute in New York the lawyer who elects to participate in the program will continue to have the same fiduciary and ethical responsibilities with respect to treatment of clients' funds that are likely to generate income for the client. The decision as to which funds may be appropriately placed in the IOLA program is left to the discretion of the lawyer to whom the funds are entrusted.

Judiciary Law § 497(5) expressly provides that "No attorney shall be . . . held to answer for a charge of professional misconduct because of a deposit of moneys to an IOLA account pursuant to a judgment in good faith that such moneys were qualified funds." See Judiciary Law § 497(2) for definition of "qualified funds." Accordingly, there can be no ethical impropriety in the event an attorney makes a deposit in an IOLA account under such circumstances. N.Y. State 415 (1975); cf. N.Y. State 323 (1974); N.Y. State 328 (1974).

For the reasons stated, the question posed is answered in the affirmative.
