

LAWYERS TRUST ACCOUNTING GUIDELINES

1. Introduction

1.1 The NZLS has issued these guidelines to assist lawyers with providing a system for handling client money and valuable property, and for administering trust accounts in law practices. The system is relatively simple and is designed for use by lawyers or their accounting staff. Although these guidelines are not mandatory, compliance with them will generally ensure compliance with the trust account provisions of the Lawyers and Conveyancers Act 2006 (“the Act”) and the Lawyers and Conveyancers Act (Trust Account) Regulations 2008 (“the Regulations”). Lawyers and others are welcome to contact the NZLS with suggestions for improving these guidelines.

1.2 Other trust accounting systems may also comply with the Act and the Regulations. Lawyers who use alternative systems must take care to ensure that the procedures they have adopted comply. Where your trust accounting system departs from these guidelines, we recommend that you clearly document the differences and justify the reasons for them.

1.3 The guidelines give practical information in relation to the following matters:

- The difference between a trust account and trust account records.
- The records required to operate a trust account.
- Procedures to follow when you receive trust money.
- Procedures to follow when you pay trust money.
- Reconciliation of trust account records.
- Reporting requirements.
- Interest Bearing Deposit Accounts.
- Miscellaneous matters, including lawyers’ trustee companies, withholding tax and attorneys for sole practices.
- Accounting control systems, security and retention of records.
- Issues of particular concern to Trust Account Supervisors.

1.4 The guidelines also provide a number of sample forms and registers as appendices.

1.5 The procedures suggested in these guidelines are based on a simple manual system of trust accounting. Clearly many lawyers prefer to use computerised trust accounting systems. However, there are two good reasons for basing the guidelines around a manual system. First, some lawyers still have manual systems. Many of these practices do not employ a specialist trust accountant and they are therefore most in need of detailed guidelines. Second, the principles of trust accounting are the same whether the system you use is manual or computerised. Any accounting software package should incorporate all the features set out in these guidelines. The guidelines are therefore relevant to both manual and computerised systems. Where a system is computerised, methods will be adapted to the system but the requirements will be generally unchanged.

2. Definitions

(Section 6 of the Act; Regulation 3)

2.1 In these guidelines, unless the context otherwise requires –

- “Act” means the Lawyers and Conveyancers Act 2006 and section references are to the Act.
- “Regulations” means the Lawyers and Conveyancers Act (Trust Account) Regulations 2008.
- LNCR means the Lawyers and Conveyancers Act (Lawyers: Nominee Company) Rules 2008.
- RCCC means the Lawyers and Conveyancers Act (Lawyers: Conduct and Client Care) Rules 2008.
- Terms defined in the Act or Regulations have the same meaning for the purposes of these guidelines.
- NZLS is the New Zealand Law Society.

3. Trust accounts

(Sections 6, 110, 299 of the Act; Regulations 3, 6)

Trust accounts

3.1 A trust account is defined in section 6 of the Act as meaning, in relation to a practitioner or incorporated firm, "any trust account at a bank in New Zealand that is a trust account in the name of that practitioner or incorporated firm".

3.2 Trust bank accounts must be designated "trust account", and you must put the bank and other interested parties on notice that the money in each trust bank account is trust money.

3.3 You must nominate trust bank accounts (other than Interest Bearing Deposit (IBD) Accounts) by written notice to the bank that holds the accounts. The bank will credit 60% of the notional interest calculated on that trust bank account to the Lawyers and Conveyancers Special Fund Account. The money in the Special Fund is distributed to the Legal Services Agency to fund community law centres. The bank retains the other 40% of the interest in lieu of bank charges on the nominated trust bank account. Accordingly, when you have nominated your trust bank accounts to the bank under section 299 of the Act, the bank, under section 301(5) of the Act, is not entitled to charge bank fees in respect of those accounts.

Errors and overdrafts

3.4 The trust bank account is the repository for client money. Therefore, it should never be overdrawn, nor should it be at risk of being overdrawn, for example, by paying out from a client's cheque where there is a possibility of it being dishonoured.

3.5 Where an inadvertent overdraft or other error occurs, it must be corrected promptly. Pending correction, any overdrawn balance must be made good from the practice's own funds (Regulation 6).

3.6 Overdrafts that are caused by administrative or accounting errors and promptly corrected should be reported briefly in the monthly certificate as an exception under Item 2.

4. Trust account records

(Sections 6, 111, 112 of the Act; Regulation 11)

4.1 Trust account records are the records that a practice must keep in relation to its trust account. The Act and the Regulations require you to keep trust account records that are up to date, clearly showing the amount of trust money held for each client, and that are secure against retrospective alteration or deletion.

4.2 All entries in the primary records must be dated and include references that identify their source and destination and enable them to be traced backward or forward, as the case may be (Regulation 11(3)).

4.3 The records described in this chapter are necessary to maintain a basic set of trust account records, suitable for a small trust account. This system, once established, can be extended or adapted to deal with larger volumes. Trust account records include :

- Trust account receipt book, or equivalent records (refer guidelines 5.5 to 5.7).
- Bank deposit supplement book (refer guideline 5.8).
- Trust account chequebook and electronic payment reports (refer guidelines 6.5 to 6.7).
- Trust account cash book summary or control account (refer guideline 4.4).
- Trust account journal (refer guidelines 4.5 to 4.10).
- Client trust ledger accounts (refer guidelines 4.11 to 4.16).
- Trust bank account statements.
- Trust account bank reconciliations (refer guidelines 7.1 to 7.6).
- Receipt book register.
- Records of valuable property received and held.
- Nominee company and contributory mortgage records.

The above is not intended as an exhaustive list of trust account records.

Trust account cash book

4.4 The trust account cash book is the link in the system between prime entries (receipts, cheque butts and entries originating in bank statements), and the trust account ledger and month-end reconciliations. A sample format is as follows:

Inwards Cash Book

Date	Receipt No.	Particulars	Client a/c credited	Receipt value	Amount banked
July					
1	2301	ASB Bank – mort. advance	J Smith		127,500.00
1	2302	J Smith – cash contrib	J Smith	24,300.00	
1	2303	M Brown – cash in house	F Brown Est.	47.50	
1	2304	New Lynn Motors – proceeds 2 cars	F Brown Est.	37,440.59	
1	2305	T Johnson – on a/c costs re assault charge	T Johnson	755.00	62,543.09
2	2306	R Jenkins – bal fees owing	R Jenkins		75.00
3	2307	G Evans – balance fees	G Evans	39.95	
3	2308	First National – dep \$30,000, less commission \$17,700 on 801 Long Road	H Jones	12,300.00	12,339.95
<i>Etc</i>					
31	2399	Downtown Auctions – proceeds furniture	F Brown Est.	750.00	
31	2400	S Read – Rent 9 Short St, 15 June-20 July	Myers Trust	1,090.00	
31	2401	K Lyall – Int. on loan 8% on \$13,000 for qtr to 31/7	H Kelly	260.00	2,100.00
	3244	Cheque cancelled (see note)	M Smith est.		3,756.43
					<u>208,314.47</u>

Notes:

1. A receipt banked separately or directly to the trust bank account will be shown in the bank column. Where two or more cheques are deposited to the bank, the individual amount will be shown in the "Receipt value" column and the total amount of the deposit extended to the "Amount banked" column.
2. When a cheque is cancelled after recording, it should be reversed by recording it in the Inwards Cash book and in the client ledger account as a credit.

Outwards Cash Book

Date	Payment No.	Particulars	Client a/c debited	Electronic payment value	Cheque value
July					
1	3470	Horne & Partners – settle purchase 5 Clover Avenue	J Smith		150,420.75
1	3471	Village Carpenters Ltd – repairs to 9 Short St	Myers Trust		458.00
1	3472	ACC – rates & water rates	J Smith		534.78
2	3463	IRD – balance of income tax	H Kelly		1,544.27
3	030710	AMEX – balance owing at date of death	F Brown Est.	15,633.95	
4	3464	A Robinson – balance of funds	A Robinson		60.00
4	040710 etc	J Smythe – balance of funds	J Smythe	100.00	
4	2295	Unpaid item reversed by bank (see note)			3,842.75
				<u>15,733.95</u>	<u>156,860.55</u>

Notes:

1. The "Payment No." column is used to record an electronic payment reference or cheque number.
2. If a bank advises that a cheque deposited or automatic payment has not been paid by the bank on which it was drawn and that the item has been debited to the trust bank account, this unpaid receipt should be recorded in the Outwards Cash Book and debited to the client's ledger account.

Cash Book Summary (or “Cash Control Account”)

Opening Balance at 01.07.2010		49,324.48
Receipts as per Inwards Cash Book		<u>208,314.47</u>
		257,638.95
Payments as per Outwards Cash Book		
Electronic	15,733.95	
Cheque	<u>156,860.55</u>	<u>172,594.50</u>
Closing balance at 31.07.2010		<u>85,044.45</u>
As per list of balances		

Trust account journal

4.5 The trust account journal is used to record transactions of the following type:

- Transfer of funds between two clients.
- Transfer of funds between two accounts of one client.
- Transfer of fees, disbursements or commissions from the client's account to the practice's float account in the trust ledger.

4.6 The trust account journal can be kept in books that can be purchased from any stationer or on loose-leaf requisition forms. In either case, the following information must be recorded:

- Date.
- Folio number. Each journal entry must be numbered consecutively for cross-referencing purposes.
- The name of each ledger account debited and credited.
- The ledger account numbers. These are recorded in the journal when the entry is transferred to the ledger.
- Amount.
- Narration.

4.7 Journal entries must include, by way of narration immediately under the entry, a complete and comprehensible explanation of why the entry is necessary, including cross-references to other entries or other documents.

4.8 Journal entries are capable of removing from or adding to client entitlement to trust funds. For this reason, the system of internal control should ensure that only authorised journal entries are posted to the trust account ledger. As part of that system, the Trust Account Supervisor should scrutinise each page as it is completed and indicate approval by signing the bottom of the page.

4.9 Where loose-leaf journal entries are approved, they should be sequentially numbered, signed by the appropriate person to authorise them and filed for easy reference. In such cases, a journal transaction report should be produced from the computerised trust accounting system for scrutiny as in 4.8 above.

4.10 A sample format is as follows:

Trust Account Journal

Date	Folio	Name of a/c	Ref	Dr	Cr
2010					
July 3	0001	J Smith	38	820.00	
		Firm's a/c Narration: BOC 78 03.07.2010 for purchase	145		820.00
July 4	0002	P & R Groves R Groves – share of Matrimonial Property Narration: Settlement as per deed dated 30.06.2010	23 29	127,500.00	127,500.00

Trust account ledger

4.11 The function of the trust account ledger is to record the entitlement of each client to the funds held in the trust bank account. The ledger contains one or more accounts for each client, recording every movement of money into or

from the funds of that client and the resulting balance available. It is therefore critical to keep the trust account ledger accurately.

4.12 The trust account ledger in its simplest form is a set of ruled cards as shown below. The cards are kept together, in alphabetical order of client. Inactive cards are kept in a separate section, also alphabetically. Where a client or groups of clients comprise varying individual interests, the practice must ensure that the money relating to each individual interest is separately accounted for. This is commonly achieved by opening separate accounts or sub-accounts for each matter. Most trust account computer packages provide for this.

4.13 Entries to the ledger cards are "posted" by transcribing the details from the prime record (receipt book, chequebook or journal) and a reference entered in the posting mark column such as the cheque number, receipt number or journal page or requisition number. Payments from the trust bank account are debits and receipts into it are credits. As each entry is made, the resulting balance of the client's funds is entered in the right-hand money column.

4.14 All entries in the trust account ledger, and in other accounting records that are the source of such entries, must be dated. They must include cross-references that identify their source or destination to enable each entry to be traced backward or forward as the case may be.

4.15 The trust account ledger is self-balancing. When all entries are made and the balances correctly calculated, the total of the list of balances should be the same as the reconciled balance of the trust bank account (refer to guideline 7.6).

4.16 A sample format is as follows:

Trust Ledger

Howard & Co, Lawyers

Client: J Smith

Ledger card No. 38

	Details of Transaction	Ref	Debit	Credit	Balance
01.07.10	ASB Bank – mortgage advance	2301*		127,500.00	127,500.00
01.07.10	J Smith – cash contribution	2302*		24,300.00	151,800.00
01.07.10	Horne & Partners – settle pchse 5 Clover Ave	3470**	150,420.75		1,379.25
01.07.10	ACC – rates and water rates	3472**	534.78		844.47
01.07.10	Howard & Co – fees and disbs BOC 78	J/27***	820.00		24.47

* = Receipt No.

** = Cheque No.

*** = Journal No.

Obligation to keep records of clients' valuable property

4.17 Valuable Property – sections 111 and 112 of the Act. You must keep records of any valuable property held in trust on behalf of any person (section 112(1)). The records must be in a form that can be inspected, and (i) describe the property received; (ii) show the date on which the property was received; and (iii) if the property has been disposed of, give details of the disposition of the property, including the date on which and the person to whom the property was disposed of.

4.18 Valuable items include:

- Documents of title to assets.
- Bearer securities (that do not require a signature to transfer).
- Saleable chattels such as jewellery.

4.19 A suggested form of record of valuable property is shown in Appendix C. Those practices with computer-based systems that provide for recording valuable property lodged with the practice should use those systems.

4.20 Shares held in your control under the FASTER system fall within the definition of valuable property. You should therefore be mindful of your obligations under sections 111 and 112 of the Act to account to the person on whose behalf the property is held and to keep proper records in relation to the property.

4.21 On occasion, clients will ask practices to hold saleable chattels as per guideline 4.18 above. In a limited number of cases this may be appropriate but, unless there is no practical alternative and the practice has secure facilities, it is preferable to refer clients to their banks for this service.

Land titles under Landonline

4.22 For guidelines for the use of Landonline, refer to the quick link on the Property Law Section's website at www.propertylawyers.org.nz

Lawyers nominee company mortgages

4.23 All transactions, both principal and interest, relating to nominee company and contributory mortgages are to be recorded in the practice's trust account records. Together with the related security and other records, they are subject in all matters to the Act, the Regulations, the LNCR and the RCCC.

4.24 The accounting records to be maintained include:

- Mortgage cards or computer equivalent records in the name of the mortgagor recording clearly:
 - particulars of the mortgage, including date of maturity, rate of interest, dates interest payable, mortgage number and title reference;
 - principal advanced to the mortgagor and repaid;
 - interest due by the mortgagor and interest paid;
 - names of investors and amounts contributed by each;
 - changes in investors showing dates, names and amounts;
 - interest credited to investors.
- A register of clients' investments in nominee company mortgages recording the investments of each client in such mortgages. This register may consist of a set of cards or computer equivalent records.
- A nominee company mortgages control account.

4.25 All trust monies invested on behalf of clients in nominee company mortgages and all repayments to clients of such monies should be recorded by way of journal entry in a separate trust account journal which should be divided in sections for:

- Advances from clients.
- Repayments to clients and transfers of interest.
- Changes in investors.

Sectionalising eliminates the need for narrations and facilitates postings to the mortgages control account, the mortgage cards and the register of clients' investments.

In addition to postings each day from the journal to clients' trust ledger accounts, as at the end of each month the total advances for the month must be posted to the debit of the mortgages control account and the total repayments of principal for the month must be posted to the credit of this account.

The balance of the mortgages control account must be agreed at least monthly with:

- The total mortgage advances outstanding as per the mortgage cards.
- The total amount of trust moneys invested in nominee company mortgages according to the register of clients' investments.

A clear record of action in accordance with the foregoing should be checked and signed each month by the Trust Account Supervisor and be suitably filed so as to be readily available to be conveniently and properly audited or inspected.

4.26 Similar records to those in guideline 4.25 above should be maintained for contributory mortgages, in a manner that enables them to be conveniently and properly audited or inspected.

4.27 A file for each mortgage should be maintained containing the investment authorities, valuation reports and other information given to investors, and any correspondence to investors concerning defaults.

Other records

4.28 Files should be maintained for trust account bank statements, bills of cost debited to the trust account ledger and month-end balance working papers, in chronological order.

4.29 Any standing authorities should be kept alphabetically on a permanent file where they will be accessible. Authorities relating to individual payments or debit journal entries should be numbered in accordance with the entries they support and filed in the same order.

5. Receiving trust money

(Sections 110 to 112 of the Act; Regulation 12; refer also guidelines 8.6 to 8.9 on money laundering)

5.1 When you receive trust money, the following steps (properly followed) should ensure that you comply with the Act and the Regulations.

One person should be responsible for receiving trust money

5.2 For proper accountability, one person should be responsible for receiving and recording trust money, and should have custody of that money. This should include appropriate lock-up facilities, up to the point where it is handed over for banking. You should arrange suitable relief during lunch hours, etc.

Enter the receipt of the trust money in the trust account receipt book

5.3 When trust money is received, it should be entered in the trust receipt book or computer equivalent record.

5.4 Receipts should be written even where the payer does not request a receipt (unless a different system is used, as discussed in guideline 5.6). If not issued, the top copy receipts should remain in the book. The receipt must always be issued when the money is received in cash or the payer requests it. Cash should always be counted in the presence of the payer at the time it is handed over so there is no doubt as to the amount received. The receipts are to record full information about the parties involved and on the nature of the payment as indicated by the layout of the form. The receipt writer should ensure that s/he has sufficient information to complete the receipt form fully.

Trust account receipt book or equivalent records

5.5 Trust account receipt records record and acknowledge the receipt of trust money. Trust receipt forms (where used) must be in the approved design and either printed by the practice's own system or obtained from a supplier authorised by the NZLS. That design includes the name of the practice on the receipt form, provision for all the required information as to date, amount, purpose and parties, and a fast copy to remain in the book (Regulation 13 and Appendix A).

5.6 Any type of system other than a trust account receipt book for recording the receipt of trust money must:

- include the equivalent information;
- be secure against any retrospective alteration or deletion; and
- provide for issuing receipts in the prescribed form when requested by the payer or when money is received in cash.

5.7 Trust receipt records should provide a reliable and tamper-proof numerical sequence of entries to ensure that none can be "lost" from the sequence. Money received must be recorded in the receipt book promptly. The trust account receipt book has an important role in providing a complete, accurate and secure record of money received. Any alternative recording system (see guideline 5.6) must therefore be of a high standard.

Bank deposit supplement book

5.8 The bank deposit supplement book keeps a detailed record of the composition of each banking (refer Appendix B).

Trust money received in the form of a cheque should be crossed

5.9 If you receive trust money in the form of a cheque that is not crossed, you should cross the cheque with a stamp that states that the cheque is payable only to your practice's trust bank account (naming the bank and branch).

Cheques intended for third parties

5.10 You may receive cheques that the client has directed you to pass on to a third party such as Inland Revenue. Such cheques will usually be made out to the third party. In these cases, you should make entries in your valuable property records required under section 112(1)(b) of the Act, recording full details of the cheque, the date on which it was received, and details of the disposal of the cheque including the date on which, and the person to whom, the cheque was disposed of. One option is to record this information in a register of third party cheques. The format of the suggested register for valuable property (see Appendix C) could be adopted for this purpose and modified as necessary.

Post-dated cheques

5.11 Post-dated cheques for the trust bank account should be recorded as they arrive in a suitable record of post-dated cheques. Each cheque should be marked off when banked and recorded at that stage through the inwards cash system. A sample format is as follows:

Date rec'd	Amount	Drawer	Payee	Cheque		Client	Trust receipt written		Other method of disposal
				No.	Date		No.	Date	

Pay the money into the trust bank account

5.12 Subject to guidelines 5.10 and 5.11, you must pay all trust money that you receive into your trust bank account. Trust money should be banked promptly, daily where practicable.

Keep the trust money separate from other money until it is banked

5.13 Trust money received must be held separately from other money until banked and must not be used as a means of cashing other cheques.

Banking reconciliation

5.14 Bankings should be reconciled against receipts as follows:

- Agree the money on hand with the total value of the receipts issued and note the total opposite the last receipt issued.
- Calculate the banking to the same cut-off point and agree the banking with the total receipts.
- Show the reconciliation clearly in the trust receipt book.

This process will ensure that money received is confirmed as correct and agrees with the amount banked.

Automatic payments and direct credits

5.15 Where you arrange for trust money to be paid to you by way of automatic payment, direct credit or other electronic means, you should ensure that the payer is provided with full and correct details of the trust bank account to be credited, the purpose of the payment, etc, as appears in the trust bank account statement. The best way to achieve this is to send the payer an encoded bank pay-in slip. The record of each credit received in the bank statement should then comply with guidelines 5.5 to 5.7.

5.16 You do not have to send a receipt to the payer unless you are requested by the payer to do so, as the record in the trust bank account statement should be sufficient.

5.17 You must keep suitable records of all such arrangements, including copies of automatic banking authorities. This will ensure that if the arrangement changes, you will be able to retrieve the information you require to effect those changes (for example, if you change your bank).

5.18 You should be aware that banks might reverse electronic money transfers and exercise due care in making any payment in respect of trust money received electronically.

Transfer of funds between clients

5.19 Funds transferred in transactions between clients must be traceable. Where money is received from a client for transfer to the account of another client, the money should first be credited to the payer client's account before being transferred to the other client's account. Evidence of authority to transfer funds must be held before the transfer is made.

Trust money may be paid to Interest Bearing Deposit (IBD) Accounts

5.20 Trust money may be deposited in an IBD Account with a bank, by transfer from the trust bank account. IBD Accounts are discussed in guideline 9.

5.21 A building society is not a bank (see definition of bank in section 6 of the Act) and therefore maintaining building society accounts for client money is in breach of section 110(1)(a) of the Act. To make use of a building society for clients' interest bearing deposits, practices must first have authorities from clients and have made the disclosure required by RCCC 3.4(c) as to exclusion from Lawyers' Fidelity Fund cover.

6 Payments from trust money

(Section 110(1)(b) of the Act; Regulation 12)

You must have client authority

6.1 You must make transfers or payments from a client's trust money as the client directs, ie, only with instructions (or some other authority) from the client to make the transfer or payment. You should therefore obtain and hold on file a signed authority from the client for the payment or the series of payments. Alternatively, where you act on other than a signed instruction (eg, a telephoned instruction), you should send a written report the next day to the client and keep a copy of the report on the file.

6.2 The only situations where express client authority is not required are:

- where the payment is to the client; or
- where the transfer is to the client's interest bearing deposit account; or
- where the authority is inherent in other documents (such as a will or agreement for purchase of a property).

There must be sufficient funds

6.3 You must not make transfers or payments from a client's trust money unless the client's ledger account has funds that are available for the purpose. In some cases this may include funds that you advance to the client account from your own funds to cover disbursements such as filing fees. Some computer systems expressly provide for this.

Only one person should be responsible for preparing cheques and electronic payments

6.4 If possible, only one person and a back-up should be responsible for preparing trust account cheques and electronic payments. This person should be trained in the correct procedures and given proper authority to perform this task.

Trust account cheques and electronic payments

6.5 The only two acceptable methods of making payments from the trust account are by electronic banking transfer and by cheque. Payments effected by electronic banking transfer now significantly outnumber those by cheque. Funds on interest bearing deposit must be withdrawn and credited to the trust account before payment can be made.

6.6 Each payment must include the date, amount, account debited, payee and a short narrative as to its purpose. That information should be recorded by any one of the following methods:

- On the cheque butts which are then used as the posting medium.
- On the cheque butts but transcribed into a cash book.
- On carbon copies of cheques and attached slips.
- By way of an authorised cheque requisition (prepared before the cheque is drawn) that contains the same information. In this case, cheque requisition forms must be numbered consecutively (usually with cheque numbers) and filed in the same order.
- In sequentially filed electronic payment reports.

6.7 Every payment should be drawn in a way that permits the crediting of money only to the account of the intended payee. For electronic payments, the payee should provide their account details (eg, encoded deposit slip) and this must be checked before the payment is sent (see also guideline 11.8). For cheques, these should be printed “not transferable” or equivalent crossing and without the words “or order” or “or bearer”.

Making cheque payments to institutions

6.8 Where a trust account cheque is payable to a bank, financial institution, government department, local authority, business house or other institution on behalf of a client, that cheque should specify the name of the client. For example, it should be payable to:

“*[Name of institution]* for credit of *[name of client]*”

Obtaining bank cheques and bank drafts

6.9 Cheques payable to a bank for the purpose of obtaining a bank cheque or bank draft will normally be made out with the bank as payee, with the words added “for purchase of a bank draft in favour of...”. Depending on the system in your bank, you should record your request for a bank draft on the back of that cheque or on the bank’s form:

"*[Name of bank]* for issue of a bank cheque in favour of *[name of intended payee]*"

Arranging for trust account cheques to be signed

6.10 The person preparing a trust account cheque should ensure that the cheque signatory has sufficient information and supporting evidence in respect of the cheque to be satisfied that it has been properly drawn.

Delegated authority for signing trust account cheques and releasing electronic payments

6.11 NZLS has obtained legal advice to the effect that the law does not require that all cheques be signed or electronic payments released only by the principals or directors of practices operating a trust account.

6.12 However, it is recommended that whenever possible a principal or director of the practice should sign trust account cheques and release electronic payments because the very act of doing so represents an important part of the control of the trust account.

6.13 Where a practice gives employees the signing authority or electronic password:

- Authority should be given only to suitably knowledgeable and experienced employees and for use only in urgent cases where a principal or director is not available. Such authority should be supported by procedures to ensure that payments released are true and correct.
- Wherever possible another appropriate person should counter-sign, both carefully checking the documentation. For example, a staff lawyer who has checked that the transaction is in order for settlement might have authority jointly with the accountant who has verified that the appropriate funds are in place.
- Where practicable, in the case of a sole practice, the attorney appointed under section 44/Schedule 1 of the Act should be called upon as the preferred cheque signatory.

Procedures should include a detailed scrutiny of the payments made under such delegated authority and the related transactions immediately upon the principal’s return to the office

6.14 Practices should be aware that any such delegated authority has an element of risk, that the risk remains the responsibility of the principals or directors who must at all times take steps to minimise that risk. This might include an extension to the professional indemnity insurance policy to cover employee dishonesty.

Taking fees from trust money

6.15 You must, prior to commencing work for a client, provide that client with information in writing on the principal aspects of client service including the basis on which the fees will be charged, when payment of fees is to be made and whether the fee may be deducted from funds held in trust for the client (RCCC 3.4(a)).

6.16 You are not permitted to deduct fees from a client’s trust money unless you have provided that client with an account for the services carried out or unless the client has authorised the deduction in writing, specifying the purpose and amount (Regulation 9(1)).

6.17 You may receive funds to cover fees in advance only on the basis that these are held for the client's account in your trust account. No deduction in respect of fees may be made from funds held unless the client gives an authority for the deduction or an account has been provided to the client for the fees that are to be deducted (Regulation 10, RCCC 9.3).

6.18 There are three recommended methods of transferring money from a client's trust ledger account in payment of an invoice:

- by way of journal entry debiting the invoice to the client's trust account and crediting the practice's float account in the trust account ledger; or
- the amount of the invoice can be paid into the practice bank account by trust account cheque or electronic payment debited to the client; or
- the trust accounting software can be used to debit the client and credit the practice's float account in the trust account ledger with the fee.

6.19 Copies of invoices and trust account statements to clients should be kept in a central file in client alphabetical order (or in numerical order with an alphabetical index for each client) with further copies on the relevant client files. Invoices should be sequentially numbered and cross-referenced to the ledger entries.

6.20 Where disbursements are included in an invoice or trust account statement to a client, the disbursements should reflect only actual payments by the practice and must not include any undisclosed fee charged by the practice.

7. Reconciliations (Regulation 14)

Regular reconciliations

7.1 You should reconcile the trust account records regularly, as follows:

- Ensure that your prime receipt and payment records are up to date, including any money transfers originating in the bank statements.
- Post the entries from the prime records (receipts, cheque butts, electronic payment records and journal) to the ledger. Calculate the day-end balance for any ledger accounts with fresh entries. Write that balance in the "balance" column, opposite the last entry.
- Investigate and take action on any debit balances or other anomalies.

The frequency will depend on the system. Computerised systems can conveniently be reconciled daily. Manual records should generally be reconciled weekly or monthly, depending on circumstances.

7.2 Entries in the prime records should be made promptly and be in strict chronological order, but receipts should be recorded before payments within each day. In a manual system, pencil should be used only where it is provisional and to be later overwritten in ink. Erasing or correcting materials should not be used. Instead, you should neatly cross out an error and write the correct version next to it. The detail should be adequate for statements to be prepared from it.

Monthly reconciliations

7.3 You must reconcile the trust account as at the end of every month. The reconciliation must show clearly the outstanding items causing differences between the trust bank account balance shown in your records (ie, cash book summary or cash control account) and the corresponding balance shown by the bank statement.

Monthly reconciliations should be retained in total to form a permanent record, ie, work papers to evidence the reconciliation. Other records that should be produced and retained in support of the reconciliations include:

- Reconciliation report.
- Copy of month-end trust account bank statement.
- Unpresented cheques list detailing for each cheque number, date drawn, payee and value.
- Details of other reconciling items, eg, unbanked receipts.
- List of client balances (credits should in total equal the cash book summary or cash control account balance).
- Cash book summary or cash control account.

And separately for each interest bearing deposit facility:

- Control account for the month for each facility.
- List of client ledger balances for each facility.
- Month end bank statements for each facility.

7.4 You must complete all monthly reconciliations except for the December reconciliation by the 10th working day of the following month. The December reconciliation must be completed by the 15th working day in January.

7.5 A suggested monthly reconciliation procedure is as follows:

- Obtain the trust bank account statement to the end of the month. Ensure that your records are up to date, including any entries originating in the bank statement.
- Total the prime records for the month, transfer their totals to the main cash book to arrive at a month-end cash book balance.
- Check all entries in the bank statements to the corresponding prime records, ticking both records in the process and note any apparent errors for correction.
- Ascertain and list the outstanding items in the prime records or the bank statements (see previous bullet point) and any brought forward from the previous month's bank reconciliation. For example, a cheque drawn in July but not presented by 31 July, or a deposit on 31 July credited by the bank on 1 August, will be outstanding items and will feature in the bank reconciliation at 31 July.
- Prepare the bank reconciliation. Ensure that the bank reconciliation agrees with the cash book balance.
- Write up prime records and post the entries to the ledger, to the last day of the month (and no further).
- Ensure all journal entries for the month have been fully processed.
- Unidentified deposits are funds deposited to the trust account where the identity of the depositor is unknown. These should be itemised on the bank reconciliation for prompt follow-up action.
- Prepare a list of client balances in the ledger at month end and agree that total with the month-end cash book balance.
- If the cash book disagrees with either the bank reconciliation or the ledger total, recheck that record first. Note the amount of the discrepancy as this may be the amount to look for.

7.6 A sample month-end bank reconciliation is as follows:

Sample bank reconciliation as at 31 July 2010

Balance as per bank statement as at 31 July 2010		\$83,129.45
Add deposit not credited, Receipt 5123-9 – 512401 credited 01.08.2010		2,100.00
		85,229.45
Less unrepresented cheques		
303345 27.04.2010	25.00	
303532 31.07.2010	60.00	
303533 31.07.2010	<u>100.00</u>	<u>-185.00</u>
Balance as per Cash Book Summary (or “Cash Control Account”) at 31 July 2010		\$85,044.45

Unclaimed or unexplained balances

7.7 Unless otherwise directed, you have a duty to pay to the client any balance of money held after the task for which it was held has been completed. The procedure for reporting to the client and closing the file will normally include paying out any balance (section 110(1)(b) of the Act; Regulation 12(7)).

7.8 Where an unexplained balance remains it may be due to disbursements allowed for but not yet paid or an estimation difference in costs or disbursements. Its origin should be identified and the amount taken as legitimate costs or paid to the client as appropriate.

7.9 Unclaimed balances (commonly called dormant or stale balances) retained in the trust ledger should be noted and regularly reviewed. Where you cannot find a person on whose behalf you are holding trust money, and you do not have authority to pay the money to any other person, you should follow the procedure set out in section 337(2) – (4) of the Act (Payment to Inland Revenue). Good accounting practice requires any trust account balance left over to be dealt with promptly so as to avoid such situations.

8. Reporting requirements (Regulations 12(7) and 17)

Reporting to clients

8.1 When trust money has been deposited in your trust bank account, you must provide to each client a complete and understandable account of all trust money handled:

- in respect of ongoing activity, at intervals of not more than 12 months;
- in respect of transactions which are not completed within 12 months, at intervals of not more than 12 months; and
- in respect of all other transactions, promptly upon or prior to completion of the transaction.

8.2 Where a client's understanding is limited, you should (where possible) account to a person who can represent the client's interest and stand in the client's shoes as an intelligent inquiring owner of the money.

8.3 You must take reasonable steps to avoid situations where the only recipient of a statement or invoice is yourself or an associated person.

Periodic certificates to NZLS

8.4 You are required to forward a monthly certificate to the NZLS when the trust account has been written up and balanced for the month. The form of certificate covers matters such as the correctness of the trust account records and compliance with the Regulations. The NZLS distributes the prescribed form to all practices in a format that includes an identifying number for each practice. Completed certificates are due at the NZLS by the 10th working day of every month except that in January, 15 working days are allowed for the certificate as at the end of December. Where, in completing your certificate, you have a bank error that has since been rectified at the time of signing, you should regard your trust account as being in order and no exception should be reported. A list of matters to check before signing the monthly certificate is on the NZLS website at [www.lawsociety.org.nz/Trust account management/Trust account certificates/Frequently asked questions](http://www.lawsociety.org.nz/Trust%20account%20management/Trust%20account%20certificates/Frequently%20asked%20questions)

8.5 A quarterly certificate is also required from each practice on the status of all loans administered by the practice. Nil certificates are required where there are no such loans.

Money laundering transactions – reporting to Police

8.6 The Financial Transactions Reporting Act 1996 (FTRA) imposes duties on financial institutions (which includes law practices) to:

- verify the identity of customers/clients:
 - where there is a suspicious transaction; and
 - automatically in certain specified circumstances including where the amount of cash exceeds \$NZ10,000 or the foreign equivalent;
- report suspicious transactions to the Police Financial Intelligence Unit, P O Box 3017, Wellington 6140; and
- retain transaction, verification and certain other prescribed records for specified periods.

8.7 Practices come within the definition of financial institution when they receive funds for the purposes of deposit, investment or settling real estate transactions. Particular points to note in the FTRA are:

- Section 19 of the FTRA (dealing with legal professional privilege) provides that a trust account does not constitute a privileged communication for the purposes of the FTRA.
- Financial institutions are prohibited from disclosing to any person (other than the Commissioner of Police) any report of a suspicious transaction.
- The identity of the persons reporting a suspicious transaction is protected by the FTRA.

- A safe deposit service where money is held is subject to the FTRA.

8.8 If you fail to comply with the FTRA, you may commit an offence under that act. In addition, under the Crimes Act, criminal offences may be committed if you or your employees suspect that a client is using the trust account to launder money and you allow the transaction to continue. However, it is a defence if you prove that you allowed it to continue with the intention of reporting it to the police.

8.9 You should ensure that you have copies of the Police guidelines issued pursuant to the FTRA, and that your office procedures are adequate to deal with any situations that may arise. Copies of the Police guidelines can be obtained from the Financial Intelligence Unit from the above address, fax (04) 498 7405 or www.police.govt.nz/service/financial/guidelines.html

9. Interest Bearing Deposit Accounts *(Section 114 of the Act)*

Deciding whether to deposit trust money in an IBD Account

9.1 It is your duty to ensure that trust money earns interest for the benefit of the client concerned wherever practicable, unless the client instructs otherwise. When you receive trust money, you must therefore decide whether it should be deposited in an Interest Bearing Deposit Account ("IBD Account").

9.2 Where the amount of interest likely to be earned is minimal compared with the administrative cost, you may decide that it is impracticable to deposit the trust money in an IBD Account.

IBD Accounts must be separate

9.3 Each client must have its own separate IBD Account. The bank records must show that there are separate client accounts, grouped so that it is clear that all of the IBD Accounts are within the control and responsibility of your practice.

How the banks administer IBD Accounts

9.4 Banks provide "bulk deposit" facilities for IBD Accounts, as follows:

- The bank maintains separate accounts, interest and tax calculations for each client, but groups the accounts as the practice's facility.
- The bank supplies you with pads of deposit forms and withdrawal forms that can be presented at the bank or (by arrangement) faxed to the bank. However, it is more common nowadays for deposits and withdrawals to be effected by electronic transfer.
- The bank credits each IBD Account with interest as it accrues.
- At the month end, the bank produces a list of bulk deposit balances. The list includes other information such as interest credited that month.
- On 31 March each year, the bank will issue Resident Withholding Tax certificates.

IBD Account ledgers

9.5 You must open a separate section of ledger cards or computer equivalent to record clients' funds held in IBD Accounts. The trust account ledger should include a control account that mirrors the total value of the IBD Account. The IBD Account ledger provides a record of all trust money held in IBD Accounts for clients. The ledger must be reconciled with the month end information from the bank.

9.6 You should make entries to the ledger and to the Control Account (see below).

9.7 You can modify this suggested procedure to accommodate a computerised system. Some computer systems incorporate clients' IBD Account features with an automatic flow through to the trust account ledger of deposit, withdrawal and interest entries.

9.8 When the bank sends you Resident Withholding Tax certificates, you must send them on to the relevant clients for action by them in respect of their tax returns.

9.9 A sample format is as follows.

Interest Bearing Deposit Account Ledger

Client: IBD Control A/C
Ledger Card No.

Date	Details of Transaction	Ref	Debit	Credit	Balance
01.06.2010	Opening balance				747,385.49
05.06.2010	Deposit R L Howarth			75,400.00	822,785.49
	Deposit B R Jones			42,000.00	864,785.49
08.06.2010	Final withdrawal R L Howarth & final int (net)		75,432.97	32.97	789,385.49
17.06.2010	Part withdrawal B R Jones		5,000.00		784,385.49
30.06.2010	Net interest added to client accounts as per bank schedule			7,843.46	792,228.95

Client: R L Howarth
Ledger Card No.

Date	Details of Transaction	Ref	Debit	Credit	Balance
05.06.2010	Deposit			75,400.00	75,400.00
08.06.2010	Withdrawal and final net interest		75,432.97	32.97	0.00

Notes:

1. Transactions are recorded in the IBD Control A/C and the balance will be agreed with the bank statement for the IBD A/C.
2. Every entry on the IBD Control A/C will be posted to the Client IBD ledger A/C.
3. On final withdrawal for an individual client, the net interest added by the bank to the final withdrawal will also be recorded as a deposit.
4. Many banks credit interest quarterly to the balance held by them on the quarter date, and it is added to the principal amount on deposit. Hence this net interest must also be added to the individual IBD client ledger A/C as per the bank schedule and the total recorded as a deposit in the IBD Control A/C.

Transfers to/from IBD Accounts

9.10 The deposit/withdrawal forms supplied by the banks should be used wherever possible as the authorising document, signed by a trust account cheque signatory and faxed to the bank for action. The bank should then debit or credit the trust bank account, avoiding any need for cheques and the greater risks associated with them. There should be an instruction to the bank that withdrawals are to be credited only to the trust bank account.

9.11 Withdrawals should be recorded in the receipt book (or equivalent record – refer guidelines 5.5 – 5.7) similarly to a direct credit. One receipt for bulk withdrawal will suffice, with a copy of the schedule attached to it for posting purposes.

9.12 Where online banking is used, the procedures in guideline 9.10 should be appropriately modified.

9.13 Where practicable, all trust bank accounts should be at the same bank. Particular care should be taken where the IBD Account and trust bank accounts are in different banks.

10. Miscellaneous matters

Client bank accounts

10.1 The power to operate a client's bank account will generally take the form of powers of attorney, trusteeships or signing authorities with access to chequebooks or equivalent.

10.2 Where in the course of practice you are administering a client's bank account, you must account properly to that client and keep records to the same standard as required in respect of other trust money (sections 110(3)(b), 110(1), 111(1), 112(1)(a) of the Act; Regulation 11).

Nominee companies and contributory mortgages

10.3 If you operate a nominee company, you must comply with the LNCR.

10.4 You must also comply with the relevant Rules and the Regulations where you receive money from a client for investment on contributory securities.

Investments under section 322 of the Act

10.5 Client money held by a practice in a trust account or in an IBD (either on call or for a fixed term), unaccompanied by any specific or discretionary investment instruction, will not be within the exclusion of section 322 of the Act but will remain covered by the Lawyers' Fidelity Fund. However, client money held by a practice in a trust account or in an IBD (either on call or for a fixed term) subject to an instruction to invest the money in some "other" investment will be excluded from cover by the Lawyers' Fidelity Fund unless the instruction relates to a loan agreement covered by section 322(3)(b), a conveyancing transaction covered by section 322(3)(c) or one of the situations described in section 322(4). Examples of investment instructions that would take funds outside the cover of the Lawyers' Fidelity Fund would be instructions to purchase shares on the stock market (ie, other than an agreement for the sale and purchase of a business, which is within the definition of conveyance under section 322(6)(a)(iii)), to place moneys with a finance company or to purchase an annuity.

If you are instructed to invest money within the meaning of section 322, you will then be obliged under RCCC 3.4(c) to advise the client in writing that the money will not be covered by the Lawyers' Fidelity Fund.

Estates and Trusts

10.6 You must administer estate and trust monies in accordance with the will, letters of administration, trust deed and directions of the trustees, executors or administrators. Any investment must be authorised by them. You must provide a statement of all trust money handled for the estate or trust at least every 12 months to the executors or trustees and, where appropriate, to the life tenant and residuary beneficiaries of an estate (Regulation 12(7)). It will be appropriate to report to beneficiaries where so instructed by the trustees or where you are a solicitor trustee of an estate. You should advise residuary beneficiaries of estates, without undue delay after probate, that they are beneficiaries, with an indication of how long the process is likely to take before distribution. Note that failure to report regularly to trustees or beneficiaries, and unexplained delays in administration, are among the most frequent causes of complaints against lawyers.

10.7 Ledgers for estates and trusts should be opened in the name of the relevant estate or trust, not in the names of the individual trustees.

10.8 The LNCR prohibit lawyer trustees and lawyer attorneys from authorising investments in a nominee company or in contributory securities unless the authority is also signed by an independent person who is not a lawyer as defined by those rules and who has authority to make the investment.

Personal transactions

10.9 Regulation 8 prohibits the use of the trust account for your (or your families' or employees') personal transactions. The exception is in property or investment transactions, which are dealt with as if for a client.

Withholding tax on interest

10.10 Where you invest funds as nominee for your clients, you may be obliged to deduct Resident Withholding Tax (RWT) from interest payments received on behalf of, or paid to, those clients. Inland Revenue has issued a booklet entitled *RWT on Interest - Payer's Guide* (IR 283).

10.11 As agent, you must deduct RWT from interest you receive on behalf of your client unless the client holds a certificate of exemption or unless the payer of the interest has already deducted the correct amount of RWT.

10.12 The correct RWT treatment depends on which of the parties hold certificates of exemption. Unless your client is a registered bank, a building society, a company formed under the Trustee Bank Restructuring Act, the Public Trust (including a wholly owned subsidiary), the Maori Trustee or a trustee company, you should sight a copy of the exemption certificate and take reasonable steps to confirm that the person is the person named in the certificate.

10.13 In all cases the certificate cannot be relied on if: there has been a notice in the *Gazette*, more than five days previously, cancelling the certificate or you have grounds for believing the person is not eligible to hold a certificate of exemption.

Dealing with RWT deducted

10.14 Where you have deducted RWT from an amount of interest received on behalf of a client, you must pay that RWT to Inland Revenue by the due date.

10.15 Pending payment to Inland Revenue, deducted RWT must be credited to an account within the trust account labelled "Resident Withholding Tax Deduction Account" or similar. These funds can be placed in an interest bearing account forming part of your trust account. You may apply the interest earned in paying your reasonable costs of complying with the RWT rules. The IRD number used should be the same as for other RWT deducted from interest income of the practice. Thus your practice will have the benefit of the tax credit.

10.16 An invoice for your reasonable costs of complying with the RWT rules (the amount of the interest) is delivered in compliance with Regulation 9 if it is prepared, processed and the original placed on your RWT file.

Payments of interest to non-residents

10.17 You must deduct Non-Resident Withholding Tax from interest payments to non-residents in all cases except where the approved issuer levy regime applies. Inland Revenue has issued booklets on *NRWT* (IR 291) and *Approved Issuer Levy* (IR 395), which deal with payments to non-residents.

Attorneys for sole practices

10.18 Pursuant to section 44 of the Act, sole practices are required to complete a power of attorney on the prescribed form, within three months of commencing sole practice. An attorney and an alternate are required. The form is available from the NZLS and is on its website at www.lawsociety.org.nz/home/for_lawyers/forms2 You should obtain the prior consent of your proposed attorney and alternate and advise the NZLS accordingly.

10.19 Whenever a section 44 power of attorney is exercised, the donee becomes a Trust Account Supervisor in terms of Regulation 16 and must be qualified as such. Lawyers who are donees and not so qualified should consider taking the Trust Account Supervisor course as a precaution. For guidance for donees, refer to the NZLS website at www.lawsociety.org.nz/home/for_lawyers/regulatory/sole_practice

10.20 Lawyers who regularly act as locum for sole practices are acting under section 44 of the Act. They should obtain powers of attorney in these situations and should have passed the Trust Account Supervisor course. That course will help equip attorneys for the variety of duties and problems they may encounter.

Foreign currency in the trust account

10.21 It is feasible for a practice to set up a foreign currency trust account to receive (say) 10 million Japanese yen and retain the funds in that currency on instructions from the client.

10.22 Banks in New Zealand can open a foreign currency account at a branch in New Zealand. Section 110(1)(a) of the Act requires client money to be "paid into a bank in New Zealand to a general or separate trust account" (of the practice).

10.23 The key points to observe are:

- If not opened as a client bank account (refer guideline 10.1), each foreign currency trust account must be part of the general designated trust bank account arrangements at a bank in New Zealand. Therefore a separate trust ledger account will be opened for each currency held for each client.
- Bank statements must be obtained for each foreign currency trust account and be retained in the trust account records.
- Most leading trust accounting software packages will allow separate cash books to be produced for Bank One, Bank Two, Bank Three, etc. Accordingly, if Bank Three is a foreign currency trust account, the bank reconciliation process is achieved in the normal way.
- Depending on the features provided by the accounting system, it might be necessary to split the trust ledger into sections reflecting the different currencies. Then, for example, the ledger accounts reflecting \$US holdings will match the record of the \$US bank account.

10.24 Some currencies such as Japanese yen will involve such large numbers of digits that you will need to check whether the software will cope with it. If not, there is always the alternative of keeping manual records for that currency.

10.25 The duty to earn interest on trust account balances (refer section 114 of the Act) applies equally to foreign currency balances. However, the rates of interest available on those currencies, and the administrative requirements, will vary markedly from New Zealand currency. In terms of section 114(b), earning interest may not be “reasonable or practicable” unless the amounts involved are large or are to be held for a long period.

10.26 It may not be possible to make payments by cheque. This will depend on the banking arrangements, but in practice it may be convenient to arrange with the bank to make electronic payments (authorised by trust cheque signatories) and to record these as entries in the trust account records in the normal way.

10.27 All the normal trust accounting requirements, including authorities for payment, duty to keep proper records and the like, apply in the same way as to New Zealand currency trust accounts.

11. Internal controls in a law practice

(Regulation 11)

Accounting controls

11.1 Accounting controls are the features incorporated into the design of an accounting system to help ensure that transactions are duly authorised and correctly and completely recorded and that money is safeguarded. In relation to trust accounts of practices, they generally comprise:

- Separation of individual responsibilities.
- Supervision.
- Controls incorporated into the design of the computer system.
- External controls, such as the Act, Regulations, Rules and Guidelines.

Where the effectiveness of some controls is limited by the smallness of an office, it may be possible to compensate for this in other ways, usually by more detailed supervision.

Separation of responsibilities

11.2 Separation of responsibilities in an accounting system involves allocating to individuals defined tasks that have the effect of proving the validity of their colleagues' work. For example, the operator who posts receipts entries to the trust account ledger effectively reviews the work of the cashier who wrote the receipts. Similarly, the legal executive preparing a settlement statement from the ledger effectively reviews the ledger entries. Separation of responsibilities should ensure that any decline in the accuracy or standard of work surfaces in the system.

11.3 The mail should not be opened, collected and sorted by people who operate the trust account. Similarly, those who are responsible for receiving or paying trust money should not be involved in posting entries to the trust account ledger or in preparing trust account journal entries. Where this is unavoidable in a small office, you must ensure adequate supervision of the relevant functions.

Supervision

11.4 Supervision means regular and systematic scrutiny by a person independent of those who perform the function being supervised. Supervision becomes more important in a small office where arrangements for separation of responsibilities are not practicable. In this case, you should exercise control by becoming familiar with and regularly reviewing key operations in the system. These include:

- Participation in the mail opening and sorting process.
- Scrutiny of the journal entries.
- Scrutiny of lists of ledger balances and the ledger accounts themselves.
- Scrutiny of the monthly reconciliations.

Vacations

11.5 Vacations are important, because they create the opportunity to detect problematic areas. A good internal control requirement is that a person in a position of responsibility be absent from the office for at least two consecutive weeks. During this period, others should detect any matters that are inconsistent with established practice. Vacations over a month end for the reconciliation clerk will enable the reconciliation to be completed by someone else thereby providing an opportunity to detect any irregularities in the reconciliation.

Computer system security

11.6 It is now common even for small law practices to process their trust account records by computer, as well as practice accounts and a number of other applications which are outside the scope of these guidelines (eg, time recording and billing). In practically all applications, there will be a need for appropriate security. Advice should be obtained and proper precautions followed in the design of any system where there is a significant risk to the practice in the event of data loss or corruption.

The following relates to computer processing of the trust account records:

System access

Many practices now operate networked systems throughout the office thus giving greater access to the various databases in use. Where this is the case there should be first level access control by password at the network entry level. Each subsequently available application software should be considered for password entry control depending on the risk presented by the data held in that application.

Access to the trust account should be controlled by passwords and should give each person only the degree of access required for his/her responsibilities. Individuals will normally have defined tasks (refer guideline 11.2) and the access which the system allows each individual should reflect those tasks. For example, the accountant would have authority for the full range of accounting entries but other staff would have access only for those types of entries that they are authorised to make. Partners or directors would normally be restricted to "read only" access as they will not be trained in data entry and that will protect them and the data from their lack of familiarity with the system.

Proper procedures must be used in respect of passwords including that they are known to only the respective users, are changed regularly, are not so simple that they might be guessed by others and the passwords of staff who leave are cancelled.

Any kind of remote access arrangements (eg, from laptops or home offices) must be similarly controlled and be reasonably secure against hackers.

Some software suppliers support their customers by means of a telephone helpdesk or by sending technicians to the site. In either case, communications with the supplier should be authorised by the Trust Account Supervisor and recorded in a log. The log will give a record of problems and service calls that can prove valuable in later disputes or inquiries and accordingly the Trust Account Supervisor should scrutinise it regularly.

Controls on input

You should ensure that proper work routines and procedures are in place sufficient to ensure that input is complete, accurate and authorised, eg:

- Daily routines, where responsibility for different tasks is clearly allocated.
- Input batches are checked and totalled before entry.
- An input control record is in use, adequate to record what has been entered and to provide a running total to confirm that shown by the computer.
- Staff training in input procedures is adequate, particularly when staff change.

Controls on output

Most trust accounting systems provide a daily summary of transactions. This should be reviewed by a senior staff person or the Trust Account Supervisor, compared with the input control record and scrutinised for any odd-looking results.

Transaction lists of receipts, payments, journals, etc are usually available in the system and should be scrutinised for any anomalies or unauthorised entries. This can conveniently be at month end when checking the monthly reconciliation. Particular notice should be taken of transaction reversals and correction entries.

Monthly lists of balances and other such information should be distributed to authors so that they can scrutinise the balances for which they are responsible and raise any queries as appropriate.

System back up and recovery

Back-up procedures should be fully documented and checked regularly to ensure they are in operation. Back-up disks, tapes or CDs should be sent offsite or placed in fireproof storage at regular intervals according to the level of transaction volume (eg, low – monthly; high – weekly or even daily).

Restoration from back-up should be tested regularly.

You should arrange for hardware facilities to be available in the event your system is damaged, destroyed or stolen in a burglary.

General

It is prudent to document the system and procedures as they apply to your office, in a form that facilitates introducing new staff to their role and minimising disruption when a person leaves.

Selection and installation of new computer systems

11.7 Before installing a system, you should carry out adequate research to ensure that a proposed installation will be suitable for the needs of your practice in all aspects of computer processing.

The NZLS Inspectorate maintains a software contact schedule that lists known available trust accounting software packages. This schedule lists software names and company contacts who can give you further information about the features and prices of their product. Before contacting these software houses, it is suggested that you consider your needs for:

- Trust accounting and reporting.
- Time and cost recording.
- Practice accounting and management reporting.
- Debtors control.
- Compatibility with other applications such as Word, Excel, Landonline and the internet.

You should then prepare a request for proposal to send to each software house selected to submit, detailing your system needs. The software house should respond with a comprehensive proposal, ideally presented to your practice in person. Before making the final choice, you should:

- Make inquiries about the vendor/author, how long the system has been in existence, how many installed sites it has in New Zealand, what arrangements and staff are available for support of your system, and the financial stability of the vendor.
- Consider the impact these changes are going to have on your existing hardware installation. Will the software changes require a major upgrade to the hardware in your office?
- Make contact direct with existing users for a frank discussion on the performance of the system.
- Confirm that the capacity of the system is appropriate to your practice and its likely future needs.
- Consider seeking professional advice before making a decision.
- Consider the extent of education and training for key staff members who will operate the system, and for users who must understand certain parts of it. Ensure this is adequate and that ongoing support will be readily available.

When converting to the new system, the following areas require attention:

- Initially training will be guided by software house personnel. Thereafter, features should be introduced on a step-by-step basis, at a rate that the staff can absorb – eg, trust accounting functions, one month; time and cost records, the following month. System transfer time is often underestimated and can be a stressful time for staff involved.
- Permanent information such as names, addresses, account codes should be entered before the planned conversion dates so that only the balance need be entered on the day.
- Consider keeping the old system ready to be restarted for a period in case the new system is not fully successful.

Desktop banking

11.8 ‘Desktop banking’ or other electronic banking transactions also require security measures. A desktop banking system for trust money should incorporate adequate safeguards in its design including:

- Transfer of funds from the trust account should require the involvement of two people specifically authorised for this purpose (ie, the person preparing the transfer and the release authority). These systems have their own bank developed release processes and these should be dovetailed with your own payment authority structures.
- Partners, directors and staff should have the same duty to preserve the secrecy of their passwords as applies in respect of EFTPOS cards.

- The ability to check payee bank account details on a payment requisitions (or equivalent) against an encoded deposit slip or client details previously recorded.
- Display of transactions on the screen or printout in advance of release, for inspection by the payment authority.
- Confirmation when funds have been transferred. This is normally a bank generated “funds sent” report, which should be retained as part of your payment support records.
- Such transaction displays, when released, to be sequentially numbered and retrievable on the screen for (say) the previous six months.
- Equivalent transaction reports with the same sequential numbers to be printed out and filed sequentially.
- The ability to store schedules of payee details for regular payments such as interest.
- Other procedures and precautions as recommended by the bank supplying the service.

Retention of trust account records

11.9 Regulation 11(5) provides that trust account records relating to a client must be retained by the practice for at least six years after the last transaction is recorded in them. There are, of course, a number of other legal obligations to retain trust account records for particular periods, such as obligations in respect of income tax and GST. No attempt is made in these guidelines to list all such obligations.

11.10 On the death or incapacity of a sole practitioner, his or her trust account records must be retained by the successor to the practice or disposed of as required by Regulation 11(5).

11.11 Unused stocks of trust account receipts, trust account cheque forms and other trust account forms should be kept in a secure place and details of holdings and usage recorded.

11.12 For detailed guidance on retention of records, refer to the NZLS website at www.lawsociety.org.nz/home/for_lawyers/resources/guidelines

12. Internal control issues for Trust Account Supervisors

(LNCR; Regulation 16(4))

12.1 There are particular issues relating to internal controls that Trust Account Supervisors should be aware of. The issues identified in this chapter of the guidelines are not intended to be comprehensive but list well-known areas of risk that all trust account supervisors should be alert to.

Lending operations

12.2 Issues may arise in respect of lawyers’ nominee company lending, contributory mortgages and single lender mortgages, particularly in cases where borrower and lender have been introduced by your practice.

12.3 You should ensure that the authorities you obtain from lenders and the information you provide to them comply with the LNCR and other relevant requirements. These formalities must be completed before the date of the advance. If appropriate, you should train a staff member to administer the lending operation and monitor that staff member's performance.

12.4 If there are significant volumes of lending, you should operate a proper loan approval system. The loan approval system may be in the form of a practice lending committee, or you may arrange to have a second partner or director review each loan before approval. That committee or reviewing partner or director should be aware that judgement might be influenced by the opportunity of earning significant fees. A record of all the decisions of this committee (or reviewing partner/director) should be circulated to all partners/directors.

12.5 The lending committee should be aware of borrowers or situations that pose a higher than usual risk to the lender, bearing in mind that a practice may often be the lender of last resort. You should ensure the lending committee members know when and how to say "no" to a proposal and that they remain firm in the face of pressure. For example, the lending committee might consider declining proposals:

- Where the value of the security and/or the borrower's ability to service the debt is dependent on the success of the borrower's business.
- Where the borrower is already heavily committed.

- Where the maintainable income of the borrower is insufficient or marginal in relation to the debt servicing commitment.
- Where the borrower is a new client whose past record is unknown.
- Where the structure of the borrowing entity is unusual or the form of ownership is complex.

12.6 You should develop lending policies to cover the following:

- Lending criteria. For example:
 - Will you lend on residential property only or on commercial property as well? Note that lending on undeveloped land generally carries a higher risk.
 - If you do lend on commercial property, will there be any reduced lending limits or premium interest rates?
 - Will you accept second mortgages? If so, what limitations will be imposed?
 - Collateral security requirements.
 - The form of valuation required, eg, a registered valuer's report or rateable value (formerly Government Valuation).
 - Borrowing maximum as a percentage of property value.
- Types of borrower. For example:
 - Will you lend to companies or trusts?
 - If you do lend to companies, will you require shareholder guarantees?
 - Will you require credit checks on borrowers?
 - Will you lend to property developers?
 - Consider mortgage debt servicing ability.

12.7 You should have a spread of borrowers. It is prudent to set limits on the proportion of total investor funds that may be advanced to any one borrower or related group of borrowers (say 10%), and on the proportion of any investor's funds that may be so advanced (say 20%).

12.8 You should monitor the status of borrowers, including defaults (even if only a few days) and any known changes in their circumstances. It is important to pursue arrears vigorously. You must report to investors under Rule 13 of the LNCr, where appropriate, and keep a file recording all decisions made and action taken on arrears.

12.9 Prior to making a lending decision, certain information needs to be obtained from the borrower. To ensure the information you require is obtained, it may be appropriate to use a loan application form. The information required needs to be determined by each practice and will also be governed, in part, by that practice's lending criteria. Borrowers' information might include:

- A statement of assets and liabilities.
- A statement of present income and expenditure.
- Sources of income (eg, employment income might warrant confirmation with the employer), and employment history.
- Whether or not the prospective borrower has been denied credit before and the circumstances.
- Availability of insurance policies, or any other collateral security.

12.10 Having obtained information from the borrower it needs to be analysed. In making a lending decision it is important to consider the borrower's ability to service the debt and the financial position of the borrower. In analysing the financial position of the borrower, some points that may be considered are:

- The extent by which income exceeds expenditure.
- The extent by which assets exceed liabilities.
- Whether the income is dependent upon the success of the borrower's business.

The key factor to consider when analysing a borrower's debt servicing ability is the ability to make interest and principal repayments pursuant to the lending agreement. This ability is likely to be determined by the borrower's income and expenditure levels.

Daily and monthly routines

12.11 The accounts clerk or computer operator should work to a daily routine of writing up and posting all transactions. It is your responsibility to ensure that this routine is followed and is not prejudiced by pressure of other work. Similarly, the monthly routine of balancing the trust ledger, reconciling the bank account, and scrutinising ledger accounts for discrepancies or unusual features should be carried out promptly by the staff and properly monitored. You should meet with the whole practice regularly to air any concerns over the trust account.

Client queries and complaints

12.12 You should investigate promptly any queries or complaints involving client money, and be alert to any that may indicate a wider problem in the practice. Note that Rule 3.8 of the RCCC requires all law practices to have appropriate procedures for handling client complaints promptly and fairly. Note also the provisions of the RCCC on “Client Service and Competence” (Chapter 3) and “Fees” (Chapter 9).

12.13 You should arrange for mail to be opened and distributed in the presence of a partner, director or senior staff member not directly involved in trust account work. This is your opportunity to detect any client dissatisfaction where it might otherwise have been suppressed. Where possible, rotate this task among the practice’s senior administrators or (if you have a small practice) your partners/directors. Those who supervise the mail opening should be strictly bound to refer any expression of client dissatisfaction to you immediately.

12.14 The principles for monitoring email correspondence are no different from those involved in monitoring “hard copy” correspondence. Accordingly, the person responsible for monitoring emails should either be a partner, director or senior staff member. The monitor should, as a consequence of their appointment, receive the ability to access electronic communications from and to the firm (including to each email address held by the firm and its authors). The monitor should inspect daily each author’s mailbox folders.

12.15 Any delegates of the monitor should be chosen bearing in mind they need the ability to understand both the content and significance of communications they are reviewing. For employment law purposes, it will be highly desirable for each firm’s email policy relating to monitoring to be published to every internal user of emails so they know they are being monitored.

Computer system

12.16 If your trust accounting system is computerised, you should monitor the operation of the system regularly to ensure that all aspects of it are satisfactory. You should ensure that daily balancing and all other routines are up to date. This is crucial where either the system or the operator is relatively new.

12.17 You should ensure that the operator is competent and has been provided with adequate guidance and documentation from the system suppliers. You should also ensure that system suppliers comply with any maintenance contract and that they respond promptly when called upon.

12.18 Where possible, you should ensure that there is a back-up operator who is capable of taking over when the regular operator is sick or on leave.

12.19 You should ensure that there is a properly maintained system for producing and filing away all of the regular reports, particularly those due at day end or month end.

Invoicing

12.20 You should ensure that all authors know and comply with the Regulations and Rules that relate to invoicing or taking legal fees from the trust account (refer guidelines 6.15 to 6.20).

12.21 Where possible, you should ensure that invoices are issued with prior approval from the client for the legal fees involved, or that invoices are adequately presented to the client.

Accounting to clients

12.22 Your practice should have systems for producing statements to clients on completion of transactions or (where appropriate) at least annually (refer guideline 8.1). You should establish and maintain a system for ensuring that all statements have been sent.

High risk clients

12.23 Experience has shown that the following types of clients are especially vulnerable and so conducive to misappropriation or other crises for lawyers, and should be given your particular attention:

- Estates or trusts where a partner or director is the sole trustee, or where the trustees do not themselves take an active part in the administration of the estate.
- Absentees, where money has been left with one partner or director to invest over a long period.
- Elderly people, whose grasp of property or financial matters is slipping and who depend on lawyers to attend to their affairs.
- Aggressive property investors who depend on lawyers for loan money. Property investors may put themselves in a situation of imminent financial failure unless more money is made available. This puts considerable pressure on lending practices to lend more, where that course of action may be inadvisable.

APPENDIX A

(Reference: guideline 5.5)

Note 1

_____ 20xx _____ RECEIVED the sum of _____ dollars and _____ cents

From _____	For credit _____
_____	_____
<i>Note 2</i>	<i>Note 3</i>
Being _____	<i>Note 4</i>
_____	_____

Receipt issued by
[Name of practice]
BARRISTERS and SOLICITORS
 or **[Lawyers]**
 Official receipt form for trust monies

\$ _____ ¢ _____

- Cash *Note 5*
 By Cheque _____
 Cashier
 Direct Credit

Code	<i>Note 6</i>	IB171029
Refs	<i>Note 7</i>	

- Notes:**
1. If remittance is by direct credit to the bank, the date of credit by the bank should be recorded even though this may cause the receipt to be out of date sequence because of delay in receiving bank statements.
 2. The name of the payer. If it is a bank cheque, enter the name of the payer who purchased the bank cheque.
 3. The name of the client ledger account to be credited.
 4. An adequate narration to be entered to record the transaction.
 5. Tick whether received by cash/cheque/direct credit.
 6. Enter client ledger account number.
 7. Record any other reference required by you – eg, initials of author.

APPENDIX B

(Reference: guideline 5.8)

DATE.....20.....

LODGED WITH:

BANK OF NEW ZEALAND**(BRANCH)**

PAID IN BY:	No. of Cheques	NOTES..... COIN.....		
TELLER:	Clearance Fee	TOTAL CASH..... CHEQUES as below		
CREDIT:	Account Number		\$	
DRAWER	BANK	BRANCH	AMOUNT	
			\$	

APPENDIX C

(Reference: guideline 4.19)

Sample register of valuable property

Page No.

Client's name:

Client or Matter No.

Held on behalf of:

Security expressed in favour of:

Date Received	Item	Face Value \$	Maturity Date	Disposal	
				Date	To Whom

Notes:

1. This format will serve for security documents as well as chattels.
2. Where a computer system includes a deeds register, that will usually meet the need.