

Lawyer Charged With Interest on IOLA Deposit

BY LAZAR EMANUEL

Attorney Skidmore represented plaintiff mother and her two children in the sale of a home in which all three had an interest. \$84,613.92 of the sales proceeds were the property of the children. Skidmore decided to deposit the entire sum in an IOLA account, the interest from which was remitted by the bank to the State's IOLA fund for disbursement to nonprofit legal service providers to support the delivery of legal services to indigent and poor persons in civil litigation. No part of the interest was paid to the children. The money remained in the IOLA account for a year and a half before the court authorized payment of the principal to the children. Skidmore stated that he thought the funds would remain in the IOLA account only three months, a period he considered short enough to justify the IOLA deposit.

Plaintiffs sued Skidmore to recover interest on the proceeds. They asked that interest be computed at a rate lower than the statutory rate, i.e., the bank rate earned by the mother on other funds deposited with a bank for a period of six months. Nassau County District Judge Kenneth L. Gartner found for the plaintiffs. *Mann v. Skidmore*, New York Law Journal, Oct. 18, 2002.

IOLA accounts are controlled by Judiciary Law §497. §497(1) provides:

An "interest on lawyer account" or "IOLA" is an unsegregated interest-bearing deposit account with a banking institution for the deposit by an attorney of *qualified funds*. [Emphasis supplied.]

What are "qualified funds?" They are (Judiciary Law §497(2):

...moneys received by an attorney in a fiduciary capacity from a client or beneficial owner...which, in the judgment of the attorney, are too small in amount or are reasonably expected to be held for too short a time to generate sufficient interest income to justify the expense of administering a segregated account for the benefit of the client or beneficial owner...

A lawyer faced with the decision whether to deposit a client's funds into an interest bearing account or an IOLA account is guided by the provisions of Judiciary Law §497(4), which lists three factors to be considered by the lawyer:

(1) the amount of interest the funds would earn over the anticipated period of deposit; (2) the cost of establishing and administering the account, including the cost of the lawyer's services; and (3) the ability of the deposit bank, through subaccounting, to calculate, segregate and pay interest separately to each client whose funds are held in the lawyer's account. Judge Gartner considered a number of bar association opinions dealing with the obligation of a lawyer to earn interest on funds of a client which are sufficient in amount to earn interest. In some instances, the failure of the lawyer to provide for interest will constitute neglect. In Formal Opinion 1995-6, the City Bar stated, "...given the size of the fund and

available interest rates, if the fund is likely to be retained for a period of a year or more, a separate interest-bearing trust account for the client may be ethically required."

In deciding whether a lawyer has been guilty of neglect in selecting an IOLA account over an interest bearing account, the court must consider the exculpatory provisions of Judiciary Law § 497(4)(b) and § 497(5). Taken together, these provisions give the lawyer virtually complete discretion in selecting the account and relieve her of any liability in damages if she has exercised her discretion in good faith.

However, there are circumstances in which a court may hold that the lawyer has abused her discretion in ignoring her obligation to place client funds in an interest-bearing account. Under those circumstances, a court may depart from the decision in *Takayama v. Schaefer*, 240 A.D.2d 21 (2nd Dept. 1998). In *Takayama*, the Appellate Division reversed a decision of the Appellate Term requiring a lawyer to pay interest on client funds deposited into an IOLA account. The court relied on the fact that the good faith of the lawyer was never questioned or raised at any point in the proceeding. The court continued, however:

This is not to say that there are no circumstances under which an attorney may be held responsible or that the safe-harbor provision of Judiciary Law Sec. 497(5) has no limits.

Judge Gartner seized upon this language to distinguish the case before him. The Judge asked:

...is the implication of Takayama's comment that there are "limits" to the safe-harbor provision, meant to indicate that if the size and duration of the deposit demonstrate the absence of the exercise of any judgment, then a...judgment "in good faith" could not have been made, and the safe-harbor protection is therefore lost?

Satisfied that the facts in *Mann v. Skidmore* required a different decision from *Takayama*, Judge Gartner awarded judgment for the plaintiffs. The Judge was clearly influenced not only by the size of the deposit and the length of time it was held, but also by Lawyer Skidmore's participation in the appointment of his colleague as guardian ad litem for one of the infant plaintiffs only a month and a half before the infant attained his majority.