7 Vital Trust Accounting Reports for Law Offices

Compliant trust accounting requires more than a few basic steps. Proper records must be maintained, and if you want to weed out potential bookkeeping mistakes, modern tech can provide a critical safeguard against everyday human error.

This guide will cover all the terms and steps you need to know, along with key reports and recordkeeping, and how your accounting software can help keep your firm compliant.

What makes legal accounting unique?

As a lawyer running a law firm, you have to have an understanding of more than just the accounting basics that an average bookkeeper would need to know. Your law practice books will be governed by a unique setup.

BUSINESS ACCOUNTING

You have to maintain the financial books for your law firm, which is an operational business. Just like other businesses, your daily accounting will include:

- Operating account (payments and expenses)
- Overhead (insurance, office rent, staff salaries, legal subscriptions, etc.)
- Your income

LEGAL ACCOUNTING

Additionally, you have to stay on top of legal-specific accounting aspects that may be passed along to clients, including a combination of:

- Billable hours
- Hard costs (advance payments for filing fees, court reporters, etc.)
- Soft costs for general business overhead (set fee or itemized)
- Managing a trust account for retainers, settlements, etc.

COMPLIANCE (VARIES BY JURISDICTION)

You need to keep accurate records that show the client money you're holding in trust is where it's supposed to be. In the event of an audit, every cent must be accounted for—and you must have up-to-date records at the ready.

All of the accounting pieces are important to do correctly to have a profitable, well-run law firm, but of all of them, **trust accounting** is the one that usually presents the biggest challenge. It's also one of the more common causes of intentional (fraud) and unintentional ethics violations for lawyers.

What is trust accounting?

Trust accounting involves keeping up-to-date ledgers for your trust accounts and adhering to compliance requirements, including three-way reconciliation. Specific requirements will vary by country as well as state/province and any additional overseeing entity.

Trust accounting workflow

In maintaining a trust account, the start-to-finish workflow generally follows this pattern:

- The client deposits funds for you to hold in the trust account.
- You do work for the client, invoice, and withdraw funds according to billed hours or expenses, leaving a clear paper trail.
- To withdraw trust funds, checks written from the trust account to your firm's operating account must include the trust account, client or matter, and purpose. **The same transfer can be performed electronically, but all the relevant information must be included.**
- Each month, once you've received your bank statement, you reconcile accounts.
- Monthly reporting must identify each matter account and balances.
- Maintain records in accordance with your local jurisdiction's requirements in case of an audit.

Types of funds in trust

There are three types of funds that you may hold in trust for your clients.

1 ***Settlement funds*** are deposited into the firm's trust account and then distributed to recipients. Ex: personal injury, real estate, etc.

2 ***Unearned income*** is money you hold in trust for the work you are going to do. It's paid out in fees you charge and cost advances.

3 ***Third-party funds*** are accounts paid by someone other than the beneficiary (i.e. family or friends).

Trust accounting records

BANK JOURNAL

This is where you keep records and details of all transactions (including voids) going into and out of your operating account. Be sure to include the following information for every transaction:

- Date
- Payee/payor
- Amounts
- Purpose
- Client identification/matter

This is where you keep records and details of all transactions (including voids) going into and out of your operating account. Be sure to include the following information for every transaction:

Note: **You may also need to keep individual deposit slips.**

TRUST RECEIPTS JOURNAL

For trust accounts, you'll want to keep the records for money coming in (receipts) separate from money going out (disbursements).

Keep track of the same details for trust transactions as you do your operating account (above). Individual client or matter accounts are tracked here. Use the receipts journal to compare deposit activity or look for a specific item.

TRUST DISBURSEMENTS JOURNAL

A record of money outgoing from the trust account, the disbursement journal can be referenced when reconciling checks or looking for a specific item.

TRUST LISTING

Also known as the trust ledger balance report, the trust listing gives you the big-picture view. It's a record of all matters and their respective balances. It lets you identify negative balances, see what funds are available, and note the last activity for each matter so you know when accounts need to be closed and funds returned.

To see an example of each of these vital trust accounting reports, view the "Trust Compliance Sample Report Package"

CLIENT TRUST LEDGER

The client trust leger puts all transactions linked to a matter in one place—it's like a mini bank account for each matter. You must always keep track of each matter's balance to show that you're staying compliant and not overdrafting the account.

TRUST TRANSFER RECORD

The trust transfer record is your paper trail for when you need to shift funds from one ledger to another—even if those funds are within the same bank account. The trust transfer record must include when the transfer occurred and its purpose.

TRUST RECONCILIATION REPORTS

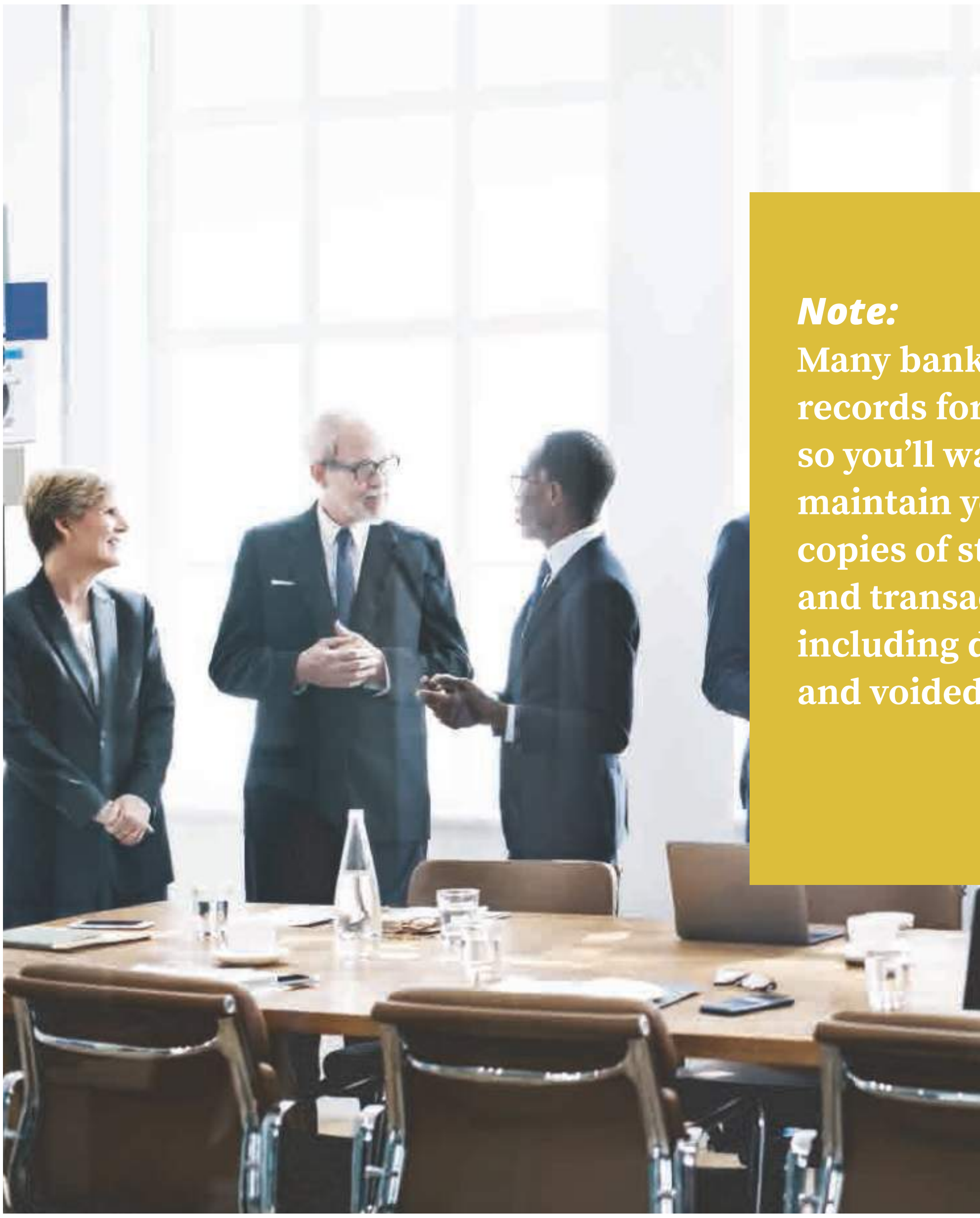
Reconciliation reports are critical to compliant trust accounting. In addition to showing balanced records, they help you keep track of cleared and uncleared items, including long-term.

And don't forget about three-way reconciliation! Here, you compare the bank balance, ledger balance, and all individual client (or matter) ledger balances.

Best practices

These seven reports need to be generated and reviewed each month. In the event of an error, it's much easier to fix when it happens—rather than at the end of the year.

It's your responsibility to know the requirements of your jurisdiction, including how long you must keep trust account records. In some places, you may need to keep records for seven years.



Note:
Many banks don't keep records for that long, so you'll want to maintain your own copies of statements and transactions—including deposit slips and voided checks.

How your tech can impact compliance

How you keep your records has a big impact on the amount of time you spend maintaining them—and makes it more or less challenging to keep on top of monthly tasks.

Written records and spreadsheets still require you to do the calculating, which makes some lawyers more likely to put things off. Generic accounting software gives you the ability to close books and run built-in reconciliation.

However, legal-specific accounting software gives the true tech advantage by helping you stay compliant with matter-centric records, trust safeguards, and compliance reporting.

Building a solid understanding of trust accounting and required records is the critical first step in staying compliant. But to streamline consistent record-keeping and guard against human errors in accounting, use legal-specific tech.

About CosmoLex

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