

**KENTUCKY LAW UPDATE**



**2025**

**ADVANCING THE PROFESSION THROUGH EDUCATION**

# **Trust Account Management**

1 Ethics Credit

Sponsor: KBA Office of Bar Counsel

**Compiled and Edited by:  
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for  
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## I. INTRODUCTION

[SCR 3.130\(1.15\)](#), formally titled “Safekeeping Property,” governs the use and maintenance of client trust accounts. Any attorney who holds funds for a client or third party must do so in a trust account, separate from the attorney’s own funds, pursuant to this rule. Every Kentucky attorney should read and understand the requirements of this rule.

## II. WHO NEEDS A TRUST ACCOUNT AND WHY

Most firms and solo practitioners will have two different types of accounts for the practice: an operating account and a trust account. The purpose of the operating account is clear; it is used to operate the office. The funds in that account are **the lawyer’s money** — earned fees to be used to pay salaries and taxes, pay utility bills and rent, and generally keep the office running. Advance fees, obtained with a proper written fee agreement pursuant to [SCR 3.130\(1.5\)\(f\)](#), formerly referred to as “nonrefundable retainers,” could also be deposited in this account, though there is a possibility some or all of those funds could have to be refunded at a later date.<sup>1</sup>

The trust account is used to hold **other people’s money**. Trust accounts serve two purposes: 1) keeping client or third-party money in a lawyer’s possession in connection with a representation, separate from money belonging to the lawyer; and 2) safeguarding the client or third party’s money. Any lawyer who accepts fees for work not yet performed, accepts payments for costs not yet incurred, holds money for a third party, or receives settlement funds **MUST** have a trust account. Common situations in which the need for a trust account arises include settlement of personal injury matters and closing real estate transactions. Payments of retainers, flat fees, or any other fees for work not yet performed must also be deposited into a trust account, to be transferred to an operating account when the work is complete and the fees are earned.

## III. BASIC REQUIREMENTS FOR TRUST ACCOUNTS

Trust accounts must be separate from the lawyer’s own accounts, whether personal or professional. The funds in these accounts belong to clients or third parties and are not to be used by the lawyer as his or her own, or that of the firm. Pursuant to [SCR 3.130\(1.15\)\(a\)](#), trust accounts must be kept in a bank in the state where the lawyer’s office is located, absent consent from the client or third party to whom the funds in the account belong. The bank

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\* Administrative Manager/Deputy Bar Counsel, Office of Bar Counsel, Kentucky Bar Association.

<sup>1</sup> Comment 11 to [SCR 3.130\(1.5\)\(f\)](#) states, “A lawyer may designate a fee arrangement as an advance fee and upon receipt deposit such funds in the lawyer’s operating account. The amount of an advance fee must be reasonable in amount and comply with [Rule 1.5](#). In the event the full amount is not ultimately earned or due to other factors, such as termination of the attorney-client relationship or is not reasonable, the funds must be returned to the client as provided in [Rule 1.15\(d\)](#).”

where the accounts are kept must have an agreement with the Kentucky Bar Association to notify it in the event any overdraft occurs on a lawyer trust account.

Though a lawyer may maintain more than one trust account, depending on the nature of the practice, SCR 3.830 requires every Kentucky attorney or firm not exempt under the rule to create and maintain “an interest-bearing trust account for clients’ funds which are nominal in amount or to be held for a short period of time so that they could not earn interest income for the client in excess of the costs incurred to secure such income...” This account is the lawyer’s IOLTA (Interest on Lawyer Trust Accounts) account and is subject to the requirements of SCR 3.830.

Pursuant to [SCR 3.130\(1.15\)\(a\)](#), complete trust account records must be kept and preserved by the lawyer for five (5) years after termination of the representation. Such records include bank statements, deposit slips, cancelled checks, client ledgers, receipts, and reconciliations. These records should be kept in a location where the lawyer can access them easily and, as stated in Comment 1, should be maintained “in accordance with generally accepted accounting practice.” The lawyer must comply with any recordkeeping rules established by law or court order, and the comment directs attorneys to consult the ABA Model Financial Recordkeeping Rule.

#### **IV. HANDLING OF CLIENT FUNDS: FIVE DUTIES**

##### **A. Safeguarding Client Funds**

Lawyers must protect client funds that have been entrusted to them, meaning they must deposit them into trust accounts at banks which have agreed to notify the Kentucky Bar Association in the event of an overdraft. It is not enough to simply keep the funds safe by, for example, placing them in the office safe. The funds must be placed in a trust account. *Chauvin v. Kentucky Bar Ass’n*, 230 S.W.3d 325 (Ky. 2007).

##### **B. Accounting for Client Funds**

When requested by the client, the lawyer must be able to account for the funds held on the client’s behalf. Lawyers should always be able to provide clients with the amount of funds being held on their behalf and show any expenditures that have been made from those funds.

##### **C. Notifying Clients of Receipt of Funds**

Lawyers must promptly notify clients upon receiving funds in which the clients have an interest.

##### **D. Delivering Client Funds**

Subject to the requirements of [SCR 3.130\(1.15\)](#) or other laws (e.g., Medicaid liens), or to an agreement with the client, the lawyer shall promptly deliver client funds to the client. This includes refunds of fees or costs that have not been earned or incurred at the termination of representation. In the event of a dispute as to what that

amount should be, the lawyer should pay the undisputed portion to the client and continue to safeguard the remaining funds until the dispute is resolved. In all cases, however, the lawyer should ensure the funds are **actually collected in** the trust account before disbursing them to anyone.

E. Segregating Client Funds

Trust accounts must be separate from the lawyer's personal and business accounts. The lawyer should not keep his or her own funds in these accounts, even if there are no client funds in them at the time, and must withdraw fees as soon as they are earned.

V. **OVERDRAFT NOTIFICATION**

As previously stated, [SCR 3.130\(1.15\)](#) requires lawyer trust accounts to be maintained in banks which have agreed to notify the KBA in the event of an overdraft on that account. When notice of an overdraft is received, the Office of Bar Counsel will send a letter to the lawyer requesting a written explanation of how the overdraft occurred. The required documentation will be the check that caused the overdraft and proof that the overdraft has been corrected. Bank statements and other additional documentation may also be required. Failure by the lawyer to respond to an overdraft notification, or a response that raises questions about whether the trust account is being properly handled by the lawyer, may result in an investigation by the Inquiry Commission.

VI. **DISBURSAL OF FEES FROM THE TRUST ACCOUNT**

Earned fees should be disbursed from the trust account as soon as reasonably practicable after they are earned. Once earned, the funds become the property of the lawyer and cannot remain in the trust account. At a minimum, disbursements should be made on a regular basis, such as every 30 days. In the case of a retainer that is being drawn upon, the best practice is to send a statement to the client showing the balance before the disbursement, the amount of disbursement, and the remaining balance being held by the attorney.

A lawyer may choose to charge a flat fee for representation and, if collected before the service has been performed without a proper advance fee agreement, such a fee must go into the trust account. As always, the fee remains the property of the client until earned. The agreement with the client, which best practices dictate should be in writing, should spell out when that fee is earned, whether it is based on the completion of a certain task or tasks (e.g., preparation of a document), the occurrence of a certain event (e.g., a court appearance), or the time expended by the lawyer. The fees should be withdrawn from the trust account as they are earned.

VII. **COMMINGLING**

Commingling occurs when a lawyer places personal funds in a trust account with client funds. A lawyer cannot leave earned fees in the trust account, nor can they deposit earned fees into it. This violates the rule even when there are no client funds present. *Merz v. Kentucky Bar Association*, 547 S.W.3d 764 (Ky. 2018). A lawyer may never use a trust account

for holding or hiding personal funds. Likewise, commingling occurs when unearned fees are deposited in an operating account rather than a trust account. Either is a violation.

Commingling is prohibited because it puts the client funds at risk and violates the lawyer's duties to safeguard those funds and keep them separate from the lawyer's own. Trust accounts are typically not subject to seizure by the IRS or other creditors of the lawyer, nor are they considered part of a deceased lawyer's estate, because the money in them does not belong to the lawyer. When the lawyer puts personal funds into a trust account, it changes the character of that account and makes all the funds in it subject to seizure until it is determined what portion of the funds belongs to the lawyer and what portion belongs to the client.

Although the best practice may be to have the bank draw all fees related to the trust account from the operating account, it is permissible under [SCR 3.130\(1.15\)\(d\)](#) for a lawyer to deposit personal funds into a trust account "for the sole purpose of paying bank service charges on that account, but only in an amount necessary for that purpose." There is no specific guidance on what amount would be considered reasonable to deposit for bank charges; however, any amount should be based on what fees the bank actually charges for things like check orders and other fees. Any amount the attorney deposits for this purpose must be tracked on its own ledger, just like fees deposited for a client. Attorneys cannot deposit money or leave earned fees in a trust account merely to act as a "cushion" to prevent overdrafts.

## **VIII. CREDIT CARD PAYMENTS**

Credit card payments for earned fees must be deposited directly into the operating account. The problem is when credit cards are used to pay for retainers, unearned fees, or advance costs, as placing those funds in the operating account, even briefly, is not permitted. According to [KBA E-426](#), there are a couple of options for handling such payments. Either the attorney can set up two merchant accounts, one of which is a trust account, and ensure any unearned fees or advance costs always go into that account. The other option is to have all credit card payments go into a trust account, then disburse the earned fees out to the operating account as soon as practicable after receiving them. If an attorney intends to accept credit card payments for unearned fees or advance costs, the attorney should consult and comply with [KBA E-426](#).

## **IX. "NONREFUNDABLE" RETAINERS**

Many attorneys collect advance fees and place them into their operating accounts, claiming they are "nonrefundable" fees or retainers. First, all unearned fees must be placed in a trust account absent a signed agreement meeting the requirements of [SCR 3.130\(1.5\)\(f\)](#). Second, as the comments and the case law make clear, no fee is ever nonrefundable. The Court clarified the misconception by amending [Rule 1.5](#), replacing "non-refundable retainer" with "advance fee." As "nonrefundable" has been removed from the Rules, it should not appear in fee agreements. Comment 11, in referring to advance fee agreements, also clearly states, "In the event the full amount is not ultimately earned, or due to other factors, such as termination of the attorney-client relationship or is not reasonable, the funds must be returned to the client as provided in [Rule 1.16\(d\)](#)."

## **X. RESPONSIBILITY**

Lawyers are not absolved from liability for trust account misconduct by delegating accounting and recordkeeping responsibilities to an employee or agent. Partners in a firm must make reasonable efforts to ensure measures are in place to provide reasonable assurances that members are following the Rules of Professional Conduct. [SCR 3.130\(5.1\)](#). Pursuant to [SCR 3.130\(5.3\)](#), supervising lawyers may be held responsible for the acts and omissions of employees. *Curtis v Kentucky Bar Assn.*, 959 S.W.2d 94 (Ky. 1998). All staff working with the trust account must be properly trained and supervised. Inexperience is no excuse, whether attributed to the attorney or staff member. This does not require an attorney to be an accountant, but it does require proper oversight and an understanding of responsibilities to clients under the rules. Also, an attorney should be the signatory on the trust account.

## **XI. THREE-WAY RECONCILIATION**

A trust account is unlike most other bank accounts in that the funds in it belong to several different people and must be tracked accordingly. Every client must have their own ledger, and if there are multiple matters for a client, then each matter must have its own ledger as well. Any funds the lawyer has deposited into the trust account to cover bank charges must also be tracked on a ledger. Every debit or credit entry on the account must be made in two places—the general ledger (or checkbook register) and the specific client ledger.

When the account is reconciled (preferably monthly), the adjusted bank balance must match the general ledger/checkbook register balance, and both of those must match the total of all client ledgers. When all three are equal, the account has been reconciled—a three-way reconciliation.

## **XII. AVOIDING PITFALLS**

- A. Retain trust account records for five years after the representation concludes.
- B. Review trust account bank statements when received.
- C. Reconcile the trust account monthly (three-way reconciliation).
- D. Send clients monthly statements with trust account balances showing all disbursements.
- E. Use fee agreements to clarify work to be performed and how compensation will be earned.
- F. Properly train and supervise anyone working with a trust account.
- G. Establish clear procedures for handling the funds on receipt and for maintaining quality control.
- H. Do not allow non-lawyers to serve as signatories on a trust account.

- I. Do not disburse funds from a trust account unless the funds are collected and available in the account.
- J. Choose clearly identifiable checks and checkbooks for trust accounts, distinct from the operating account or any other accounts held by the lawyer.



## FOR YOUR INFORMATION ...

### The Kentucky Law Update: Continuing Legal Education for All Kentucky Lawyers

The Supreme Court of Kentucky established the Kentucky Law Update Program as an element of the minimum continuing legal education system adopted by Kentucky attorneys in 1984. The KLU program is now offered in a hybrid format. The 2025 Kentucky Law Update is presented as a one-day, in-person program at nine different locations across the state. The 2025 On-Demand Kentucky Law Update is available virtually on the Kentucky Bar Association website from September 1st until December 31st. These two programs combined offer every Kentucky attorney the opportunity to meet the 12 credit CLE requirement, including the 2 ethics credit requirement **close to home and at no cost!** Judges can also earn continuing judicial education credits through the Kentucky Law Update.

This program was designed as a service to all Kentucky attorneys regardless of experience level. It is supported by membership dues and is, therefore, every member's program. The program is a survey of current issues, court decisions, ethical opinions, legislative and rule changes, and other legal topics of general interest that Kentucky practitioners encounter daily. As such, the program serves both the general practitioner and those who limit their practice to specific areas of law. The Kentucky Law Update program is not intended to be an in-depth analysis of a particular topic. It is designed to alert the lawyers of Kentucky to changes in the law and rules of practice that impact the day-to-day practice of law.

### About the Written Materials and Presentations

The KLU written materials are the result of the combined efforts of numerous dedicated professionals from around Kentucky and elsewhere. The KBA gratefully acknowledges the following individuals who graciously contributed to this publication:

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KBA Law Practice Committee	Legal Aid Society
KBA Office of Bar Counsel	New Americans Initiative
Kentucky Access to Justice Commission	Supreme Court of Kentucky

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### **CLE and Ethics Credit**

The one-day, in-person 2025 Kentucky Law Update program is accredited for 6 CLE credits, including 2 ethics credits. The 2025 On-Demand Kentucky Law Update is accredited for 9.25 CLE credits, including 3 ethics credits. One credit is awarded for each 60 minutes of actual instruction, as noted on the agendas provided on the KBA website.

The Kentucky Bar Association's 2025 Kentucky Law Update programs are accredited CLE activities in numerous other jurisdictions. Credit categories and credit calculations vary from state to state. CLE reporting information for other states will be provided at the registration desk at the in-person programs. The out-of-state information for the on-demand sessions will be available on the program website.

Kentucky judges: don't forget you can claim CJE credit for attending this program.

**REMEMBER:** Reporting attendance credits is now done online. Visit the Kentucky Bar Association [website](#) for reporting information. The activity numbers for the in-person and on-demand programs are listed on the corresponding agendas and must be used to report credits through the Member CLE Portal.

### **Evaluations**

The 2025 Kentucky Law Update is *your* program, and your input *is* valued and needed. Links to the program evaluations for the live, in-person programs will be provided to all registrants via email. A link for the on-demand evaluation will be located on the program webpage. Please take a few minutes to complete the evaluation. We appreciate your assistance in improving this program.

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