

# 1

# Governance of Lawyers and Paralegals

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After reading this chapter, you will be able to:

- LO1** Identify institutions that govern lawyers and paralegals in Canada and describe the source of their authority.
- LO2** Define various forms of business organization.
- LO3** Explain the record-keeping requirements as set out in the rules and by-laws of the law society in your province or territory.
- LO4** Understand the ethical and professional responsibilities of paralegals and lawyers as they pertain to the maintenance of books and records in the management of a legal services firm.
- LO5** Identify types of bank accounts in a legal services firm and explain their function.

## LO1 Introduction

This chapter will explore the organizations that oversee lawyers and paralegals with a particular focus on the bookkeeping and accounting requirements that govern their conduct. You need to understand the accounting process and be aware of the rules mandated by the law society in your province or territory. You must be aware of what disciplinary actions law societies take for non-compliance. Do you need insurance? What bank accounts will you need? Do you want to purchase legal accounting software that helps with financial and matter management, including trust accounting? Will you hire a bookkeeper or an accountant who can guide you in making financial decisions and preparing your financial statements?

## Role of Law Societies

Every lawyer in Canada, notary in Quebec, and paralegal in Ontario is required to be a member of a law society and to be governed by its legislation. The **Federation of Law Societies of Canada**<sup>1</sup> is the national coordinating body of the 14 **law societies** that are mandated by provincial and territorial law to regulate Canada's lawyers, Quebec's notaries, and Ontario's licensed paralegals. For example, in Ontario, the *Law Society Act*<sup>2</sup> empowers the Law Society of Ontario (LSO) to regulate **licensees**, which includes lawyers and paralegals. Authority to regulate the profession in Alberta is derived from the *Legal Profession Act of Alberta*.<sup>3</sup> Paralegals in provinces and territories outside of Ontario are not licensed at the time of this writing and must work under the supervision of a lawyer. Law societies monitor the unauthorized practice of law and can prosecute anyone practising without a licence or without professional liability insurance. While some legal matters can be performed unsupervised by legal assistants, law clerks, and other legal agents, only licenced members of a law society can give legal advice or engage in the practice of law. Law societies maintain tribunals that enforce the rules of conduct to ensure that members of the profession act honourably and with integrity.

1 Federation of Law Societies of Canada, <<https://flsc.ca>>.

2 RSO 1990, c L-8.

3 RSA 2000, c L-8.

Legal practitioners can also join associations of members of the profession, such as the Canadian Bar Association,<sup>4</sup> a professional association for lawyers in Canada, to speak for and represent the interests of lawyers. Membership is voluntary in all provinces and territories except New Brunswick, where participation is mandatory through an agreement with the Law Society of New Brunswick. Paralegals may choose to join an association, such as their provincial or territorial association or the Canadian Association of Paralegals,<sup>5</sup> to expand their skills by networking with colleagues and members who provide support and continuing education. Provincial and territorial paralegal associations also help paralegals establish links with their region's bar association. Law clerks can also join an association, such as the Association of Law Clerks of Ontario,<sup>6</sup> which provides opportunities to innovate and to share ideas and knowledge of best practices for law clerks.

## CASE LAW

### Unauthorized Practise of Law

#### *Maureen Boldt v Law Society of Upper Canada*, 2010 ONSC 3568

Maureen Boldt operated a mediation and paralegal practice in North Bay, Ontario. Between 1995 and 1998, the Law Society of Upper Canada (LSUC; now the LSO) prosecuted Boldt for practising law without being licensed, contrary to the *Law Society Act*. In April 1998, Boldt pleaded guilty to providing legal services in contravention of the Act and undertook not to do so in the future. She acknowledged that the LSUC would seek an injunction if she continued to practise law.

Despite her undertaking, Boldt continued to offer legal services to the public and was found to have acted and practised as a solicitor contrary to the law. A permanent injunction was granted restraining her from “Preparing and drafting Separation Agreements and Petitions for Divorce in uncontested and contested matters; offering and providing services in the preparation and drafting of Wills and Incorporations.”<sup>7</sup> The Court stated that it was regrettable that Boldt thought she could ignore the injunction and found that she was in flagrant breach of the previous order. The appeal court found that Boldt was in breach of the order.

An article published in the *Law Times*<sup>8</sup> reported that Boldt was sentenced to house arrest for four months and only allowed to leave her home for three hours on Saturdays, for medical appointments, and for religious services. She was not allowed to carry on her paralegal practice during that time and was ordered to pay \$35,000 in costs to the LSUC.

Boldt was denied a P1 licence to work as a paralegal by the LSUC. She passed away on August 6, 2020.

4 Canadian Bar Association, <<https://www.cba.org/Home>>.

5 Canadian Association of Paralegals, <<https://caplegal.ca/en>>.

6 The Institute of Law Clerks of Ontario, <<https://www.ilco.on.ca>>.

7 *Maureen Boldt v Law Society of Upper Canada*, 2010 ONSC 3568 at para 9.

8 “Paralegal Gets Four Months House Arrest,” *Law Times* (15 October 2007), online: <<https://www.lawtimesnews.com/news/general/paralegal-gets-four-months-house-arrest/259211>>.

## LO2 Forms of Business Organization in Legal Services Firms

In Ontario, By-Law 7<sup>9</sup> of the LSO sets out several ways lawyers and paralegals may carry on the practice of law and the provision of legal services. The form of business organization used is often determined by income tax implications as well as bookkeeping issues.

Basic forms of business organization include sole proprietorships, partnerships, limited liability partnerships, multi-discipline practices or affiliations, and professional corporations. The various modes of practice are set out in more detail on the LSO website<sup>10</sup> and should be referred to as needed.

### Sole Proprietorship

A **sole proprietorship** is a business carried on by one individual who is the owner. The sole proprietor usually makes all management decisions and is personally responsible for all the debts of the business. Many small firms are sole proprietorships. The owner pays personal income taxes on the profit made by the firm. When net profits reach higher levels, there may be tax advantages in switching to a corporate form of ownership.

### Partnership

A **partnership** is a business carried on by two or more individuals as owners. Two or more persons may find it worthwhile to combine their talents and money to form a partnership. They may own the business in equal or unequal shares, and their shares of the profits or losses in the business are usually proportionate to their capital investment in the business, as documented in the partnership agreement. All of the partners are equally liable for all the debts of the business. General partnerships have unlimited personal liability for business debts. The net income or loss of the business is allocated to the members of the partnership, who then pay personal income taxes on their share of the profits.

### Limited Liability Partnership

A **limited liability partnership** is one in which partners have limited personal liability for the debts of the business, and no partner is responsible or liable for other partners' misconduct or negligence. The name of the limited liability partnership must be registered under the *Business Names Act*<sup>11</sup> and must include the words "limited liability partnership" or "société à responsabilité limitée," or the abbreviations "LLP," "L.L.P.," or "s.r.l." as the last words or letters of the firm's name.

9 Law Society of Ontario, By-Law 7 (amendments current to 25 February 2021), online: <<https://www.lso.ca/about-lso/legislation-rules/by-laws/by-law-7>>.

10 "Business Structures" (last visited 9 February 2021), online: *Law Society of Ontario* <<https://lso.ca/lawyers/practice-supports-and-resources/business-structures>>.

11 RSO 1990, c B.17.

## Multi-Discipline Practice or Affiliation

In a **multi-discipline practice (MDP) or affiliation**, lawyers and licensed paralegals work with other professionals—such as accountants, tax consultants, trademark and patent agents, or others—who support or supplement their practice of law or provision of legal services. When a licensee and another professional enter into a formal partnership agreement, it is considered a multi-discipline partnership, which must be approved by the LSO by way of application. Licensees are responsible for the actions of professional partners and must maintain professional liability insurance for all professional partners.

## Professional Corporation

In a **professional corporation**, lawyers or licensed paralegals carry on the practice of law or the provision of legal services through an incorporated entity, but they may only do so after the company has received a certificate of authorization from their law society. Corporations operate under a government charter and are owned by shareholders. All the shareholders of a professional corporation must be lawyers or licensed paralegals who are entitled to practise law in Ontario. Incorporation does not affect the professional liability of the shareholders, and they are jointly and severally liable with the corporation for all professional liability claims against the company.

Certain tax advantages can be gained by incorporating because the corporation is taxed separately on its profits at corporate taxation rates, which are lower than the personal tax rate after a certain level of income is achieved.

## Insurance Requirements

Licensees who provide legal services to the public must carry professional liability insurance in accordance with law society requirements. A policy limit for each single claim of not less than \$1 million and an aggregate policy limit for all claims of not less than \$2 million per year are required. In the case of a limited liability partnership, coverage must be maintained for each partner in the amount required for individual licensees. Some exemptions are allowed, such as when a paralegal is working under the supervision of a lawyer who has professional liability insurance through the LSO and the paralegal is covered under the lawyer's policy. Licensees must provide written proof of compliance with their insurance requirements before they begin providing legal services and annually thereafter.

LO3

## Requirement for Books and Records in Legal Firms

Books and records must accurately reflect the financial activities that you carry out as a legal professional. All money and other property received and disbursed must be tracked.

The goal of this book is to help you understand the type of financial records required to meet your obligations and to show you how to keep these records. The focus is on a small practice; examples of transactions a licensee is likely to encounter will be used for demonstration purposes. Law clerks or paralegals who perform their duties under the supervision of a lawyer should also be aware of record-keeping requirements to assist the lawyer or law firm in meeting their obligations.

LO4

## Role of Bookkeepers and Accountants

A licensee who is not confident in their own accounting abilities will want to hire a **bookkeeper** to maintain the firm's books and records. Bookkeepers record day-to-day transactions in the appropriate accounting journals. Samples of these tasks include entering bills from vendors, paying vendors, processing employee payroll, issuing invoices to clients, recording receipts from clients, and reconciling bank accounts. The bookkeeper records financial transactions in a journal and summarizes them in ledgers created for general and trust matters. A bookkeeper will usually bring the books to the trial balance stage of the accounting process.

A **chartered professional accountant (CPA)**, who has a university degree and completes a professional education program, takes over where the bookkeeper leaves off. Chartered professional accountants prepare adjusting entries to correct the balances in ledger accounts to reflect items such as prepaid expenses and depreciation. Once the adjusting entries are completed, the accountant prepares the firm's financial statements, which include the income statement, statement of owner's equity, and balance sheet. These statements are required for income tax purposes, and the accountant can complete the tax returns for the firm. An accountant will ensure that the firm's financial records reflect relevant professional accounting standards.

Why do licensees need to learn **bookkeeping** if bookkeepers and accountants are able to do the job for them? Doing your own bookkeeping may not save much money; instead, it may actually reduce your ability to earn money. You may find yourself spending considerable time and effort on an activity that does not build your practice—time that could be better spent on servicing clients, which ultimately leads to billing fees for legal work. However, the licensee is responsible for ensuring that the persons hired maintain their records in an acceptable manner. This book introduces licensees to the essentials of legal accounting and explains why and how books and records need to be kept so that their practices conform to the requirements of their law society.

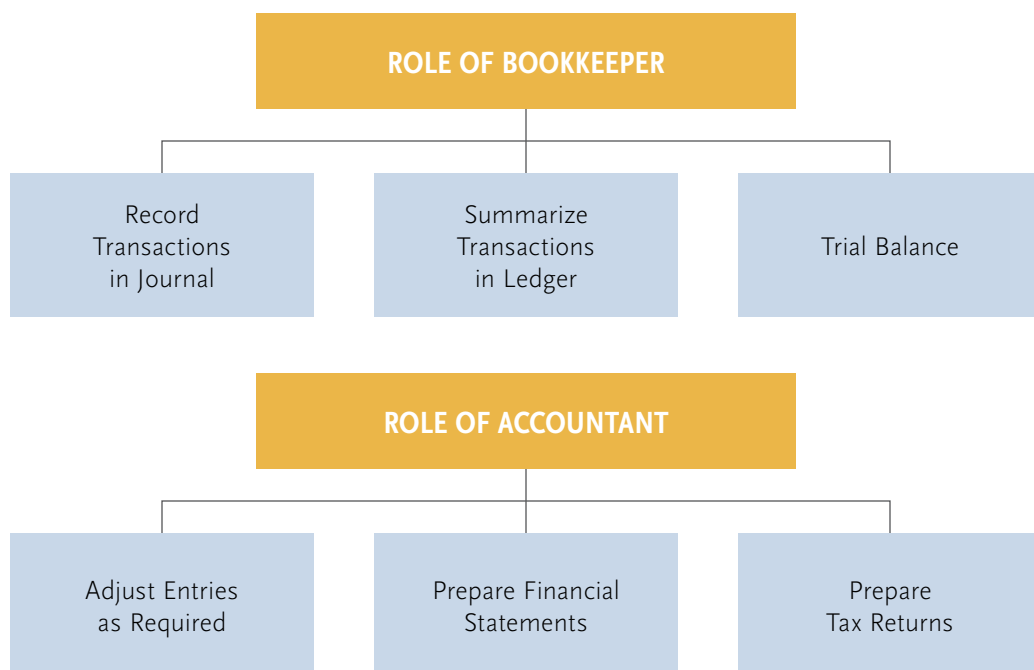


FIGURE 1.1 Role of bookkeepers and accountants

Other reasons to know basic bookkeeping and accounting principles:

- As a business owner, it is in the licensee's best interest to be able to analyze financial information for the purpose of making financial decisions in their own practice.
- As a business owner, licensees may need to explain a business plan to their bank or another lending institution, including projections of anticipated income and expenses.
- Licensees might need to understand a client's financial records in the course of litigation when financial statements are relevant to the case.
- As a community volunteer, licensees may become a member of a board of directors that must review and approve financial statements.

The following organizations require that proper records be maintained:

- The **Canada Revenue Agency (CRA)** is the agency responsible for administering the tax laws for the Government of Canada and most of Canada's provinces and territories. Alberta and Quebec have special remittance requirements for personal and corporate income taxes. Provincial and territorial governments also require maintenance of records for the purposes of income taxes and provincial or territorial sales taxes where sales taxes are not collected by the federal government.
- Law societies require the filing of annual reports and perform audits to ensure that records are correct and, in particular, that all trust funds are properly accounted for. Licensees who fail to file their annual reports on time are subject to late fees and disciplinary measures. For example, the LSO charges a \$100 late fee as well as a potential administrative suspension for late filing.
- **Law foundations** are non-profit organizations that aim to help people understand the law and provide access to justice. They require licensees to file annual reports with the appropriate law society.

## Choosing the Right Technology

Most firms now use legal accounting software to perform bookkeeping tasks. When selecting software, you must first decide which functions you want the system to perform, keeping in mind the requirements of the relevant law society as well as responsibilities for collecting PST or GST/HST. It is important to choose the right technology from the start at a cost you can afford. Some of the features you will want to consider are set out in Figure 1.2.

## Importance of Maintaining Proper Records

In addition to keeping books and records that reflect their financial activities, lawyers and paralegals have an added obligation to maintain accurate records because they hold funds and property in trust for their clients. Law societies regulate the profession to ensure that paralegals and lawyers conduct themselves in a competent and ethical manner. Their role is to protect the public, and one way they fulfill this responsibility is by auditing the records kept by law firms. An audit is an inspection of the books and records of a company, usually by an independent third party. Licensees who fail to meet the professional and ethical obligations imposed by the law society are subject to its complaints process, which can result in disciplinary action, including suspension of their privileges.

SOFTWARE FEATURES		
What operating system do you wish to use?	Mac	Windows
Pricing	Monthly	Annually
	Based on service level	
Is onboard assistance included?	Yes	No
Do you wish to manage files with the system?	Yes	No
Is the system cloud-based or on its own server?	Cloud	Server
Does the system perform:		
• General and trust banking	Yes	No
• Time/expense entry	Yes	No
• Billing	Yes	No
• PST/GST/HST reports	Yes	No
Is adequate support provided at a reasonable cost?	Yes	No

FIGURE 1.2 Accounting system considerations

Failure to maintain proper records can result in errors and an inability to meet financial obligations as they come due. For example:

- Failure to record accounts payable as bills are received results in an overstatement of income and may result in an inability to pay bills when they are due.
- Failure to stay on top of accounts receivable may result in insufficient funds in the general bank account, resulting in an inability to pay operating expenses.
- Failure to track trust receipts and disbursements in the correct client ledger could result in errors that result in a client's trust account getting overdrawn.
- Failure to maintain trust records can result in an inability to meet obligations incurred on a client's behalf and to account to clients for any funds received on their behalf.
- Failure to track income and expenses and properly report to the CRA may result in assessments and/or audits as well as severe penalties and interest charges if taxes were not properly remitted.
- Lack of knowledge concerning the business's financial situation impairs good management decision-making regarding day-to-day operations, expansion, addition of staff, and other such matters.
- Failure to maintain financial statements may result in lenders refusing applications for loans or lines of credit because lenders require financial statements in order to assess interest rates imposed on loans and qualification for loans.
- Law societies conduct regular audits of licensees. Failure to maintain up-to-date trust records can result in suspension or other action by the law society.

## Retainers

A **retainer** is an agreement between a client and a legal service provider for the engagement of legal services. The form of retainer can vary and be customized for each situation. Because clients can believe that they have retained the legal service provider based on an oral



conversation, it is important to observe client identification protocols and to document any conversation in writing.

It is a good practice to get monetary retainers from clients to ensure that there will not be any difficulty getting paid once work has started or a task is completed. The cash flow in an office is important, and having to worry about paying bills can interfere with your ability to focus on providing excellent service to clients.

Firms usually require that clients provide a **monetary retainer** when the licensee–client relationship is entered into. This is usually obtained when the client signs a retainer agreement, with the firm setting out the scope of the work to be performed and the hourly rate that will be charged by the person primarily responsible for the file, as well as the rate charged by other persons who will work on it. The retainer agreement should also set out the firm’s billing policies.

The money received from the client must be deposited into the firm’s mixed or pooled trust account (described below) by the end of the next banking day after funds are received. Money includes, by definition, cash, cheques, bank drafts, credit card sales slips, post office orders, and express and bank money orders.

A **general retainer** is not deposited into the firm’s trust account. This is money received for which the licensee is not required either to account to the client or to provide services. A general retainer should be evidenced by a written agreement with the client. As an example, it might be used when a licensee is employed to handle all collections for a client and the firm agrees to perform these collections at a fixed monthly rate. The firm will receive payment for their services regardless of whether or not the client submits any claims during a specified period. This type of retainer is not common in small practices and is carefully scrutinized by law societies.

LO5

## Bank Accounts in Legal Services Firms

At the very least, most law firms have one general bank account and one mixed or pooled trust account. It is important to understand which transactions require use of the general bank account and which require the use of the trust bank account. Mixing trust funds, which are funds that belong to the client, with general firm funds, which are funds that belong to the firm, is not allowed.

### General Bank Account

Just as individuals have a bank account that they use for their day-to-day deposits and disbursements, a business must have a **general bank account** for making deposits and paying bills. The general bank account will be opened in the name of the firm. If the firm is a sole proprietorship, the bank account will be in the name of the owner. Corporations will open such accounts in the name of the corporation. The types of funds that will be deposited into the general bank account include:

- funds that belong to the firm;
- funds invested into the firm by the owner;
- funds received by the firm for payment on bills sent to the client; and
- other receipts, such as interest income earned on the general bank account and miscellaneous income.

Regardless of the accounting system being used, care must be taken to ensure that the correct bank account is used when making deposits and paying disbursements. Firms often use different coloured cheques for their general and trust bank accounts so there is a visual cue

for the person writing a cheque. This helps ensure that disbursements are made from the appropriate account.

## Mixed or Pooled Trust Bank Account

A **mixed** or **pooled trust bank account** is a bank account into which money received from clients for certain purposes is deposited. This account is called “mixed” or “pooled” because the firm opens one bank account into which money for many clients will be deposited. The funds must be deposited into the mixed trust account because the money does not belong to the firm; it belongs to the client and is to be used for specific purposes, such as paying court fees on the client’s behalf, or the amounts may be applied to a bill for services provided to the client. How will one know what amount belongs to which client? A separate client summary called a ledger must be kept for each client so that firms always know how much money is in the trust account for each one. It is important to note that only firms who hold client money need a trust account.

### EXAMPLE

Figure 1.3 illustrates a list of funds in the trust account that are pooled. The example below explains why a record is required for the amount held for each client.

Justin Case is an Ontario paralegal who has three clients. He has received a retainer from each client and has made payments out of the mixed trust account for some clients. The bank balance for the mixed trust account is \$5,950. Justin needs to know that he has \$250 left in trust for Client A, \$700 for Client B, and \$5,000 for Client C. The best way to track this information is to have a separate client trust ledger sheet for each individual client that shows all the transactions for each client with a running balance at all times.<sup>12</sup>

If Justin did not maintain proper records and wrote another cheque in the amount of \$300 from the trust account to pay for a disbursement on behalf of Client A, the trust ledger account for Client A would be overdrawn by \$50 (\$250 less \$300). However, the bank would still clear the cheque because there was \$5,950 in the pooled account before the \$300 cheque was written. Licensees must report these kinds of errors to the law society when submitting the annual report and include an explanation as to why the error occurred.

The financial records a licensee is required to maintain for trust accounts must be entered in the account journal and **posted** (recorded) in each client’s ledger to ensure these records are current at all times.

Law Society rules of professional conduct dictate that trust accounts are to be used only for clients’ money.

If a legal service provider does not receive retainers from clients, it may not be necessary to open a trust account. Trust accounts can never be used for the personal or office use of the business owner.

Client	Receipts	Payments	Balance
Client A	300	50	250
Client B	800	100	700
Client C	<u>5,000</u>	<u>0</u>	<u>5,000</u>
Totals	<u>6,100</u>	<u>150</u>	<u>5,950</u>

FIGURE 1.3 Summary of clients and balance held in trust

## Overdraft in Trust Account

It is a good practice to place a hold on trust funds received from clients (unless paid in cash, money order, or certified cheque) to make sure there are sufficient funds in the client’s bank account to cover the cheque. Firms should confirm with their financial institution how many

<sup>12</sup> Law Society of Ontario, By-Law 9 (amendments current to 12 May 2023) at s 22(1), online: <<https://www.lso.ca/about-lso/legislation-rules/by-laws/by-law-9>>.

days it takes a cheque to clear. If a cheque from a client is returned by the bank for insufficient funds (NSF), and the licensee has written a cheque against that amount, the trust ledger for that client will be overdrawn. In addition, bank charges may accidentally be taken out of the trust account because of the NSF transaction. The bank should be directed to charge any service fees against the trust account to the firm’s general account instead.

Licensees are personally responsible for ensuring that any overdraft in a client’s trust account is corrected as soon as an error is discovered. This can be done by having the client bring in funds to deposit into the account or by the licensee depositing personal funds into the trust bank account to make up for the deficiency.

With experience, licensees develop an instinct for knowing which funds should go into the mixed trust account and which funds should go into the general bank account. If there is any uncertainty, paralegals should refer to the appropriate law society’s by-laws and rules to determine whether or not the funds belong in the trust account. The table in Figure 1.4 shows which bank account must be used for different types of deposits.

## Separate Interest-Bearing Trust Account

Another type of trust account can be set up to hold funds for only one client. This may be done on the client’s written instructions when a large amount is to be held in trust for an extended period of time. For example, if a client deposits \$20,000 with a firm to hold until a case settles and the case is expected to go on for an extended period, the client may want the interest on the account to accrue to themselves. If a client wants interest on the trust funds that a firm holds for them, they must provide written instructions to deposit such funds into a **separate interest-bearing trust account**—for example, a guaranteed investment certificate (GIC), term deposit, or other savings account—in the firm’s name in trust for them.

Opening a separate interest-bearing account for a client requires additional paperwork and bookkeeping for the licensee and is not usually done unless the return on investment is significant. Bank charges on this account would be charged to the separate interest-bearing trust account and noted as a disbursement to the client.

Separate interest-bearing trust accounts must be reconciled and included in the monthly trust comparison. If a client instructs their legal service provider to put their funds in an interest-bearing account, some additional information may be required from them, such as their social insurance number or corporation number, if applicable, as well as how the interest is to be allocated for income tax purposes. This is especially important when the funds being held are in dispute.

Mixed Trust Account	General Account
<p>Funds that must be deposited to the trust account:</p> <ul style="list-style-type: none"> <li>• money received on behalf of the client</li> <li>• money received for future client disbursements</li> <li>• money received for future or unbilled legal services</li> <li>• an overpayment of billed services—the excess payment must be either returned to the client or held in the trust account if the client instructs you to do so</li> </ul>	<p>Funds that must be deposited to the general account:</p> <ul style="list-style-type: none"> <li>• money paid on account of a bill previously sent to the client</li> <li>• reimbursement for expenses paid on behalf of the client</li> <li>• lawyer/paralegal’s or firm’s money</li> <li>• general money retainer</li> </ul>

FIGURE 1.4 Accounts for depositing funds

## Financial Institutions for Mixed Trust Accounts

The following institutions are approved for opening either a mixed trust account for all client funds or a separate account for one client:

- a chartered bank, such as RBC, TD, Scotiabank, BMO, or CIBC;
- a provincial or territorial savings office, a government-run banking institution;
- a credit union, a member-owned financial cooperative;
- a league to which the *Credit Unions and Caisses Populaires Act, 1994*<sup>13</sup> applies; and
- a registered trust corporation.

## Interest on Trust Accounts

The institution in which the account is opened must have an agreement with the relevant law foundation for the payment of interest on mixed trust accounts. The institution must also provide monthly bank statements and the originals or copies of the front and back of returned cheques, including certified cheques for all accounts.

Interest earned on a mixed trust account must be remitted to the law foundation by the financial institution in which the account is located. This is done by signing a letter of direction regarding interest on a mixed trust account, which directs the financial institution to forward interest on the account to the foundation.

It is the licensee's responsibility to ensure that the financial institution where the mixed trust account is to be opened pays interest at a rate approved by the law foundation's trustees. Most financial institutions have an agreement with the region's law foundation and are accustomed to remitting the interest as required. The law foundation then uses these funds to carry out its mandate to promote access to justice.

In Ontario, an annual report must be sent to both the LSO and the Law Foundation of Ontario by March 31 each year.

### POTENTIAL PITFALLS

- **Potential pitfall: Not keeping accurate, complete, and up-to-date books and records.**
- **Possible fallout:** In 2017, a Canadian legal firm was fined \$25,000 for failing to provide documents to the LSO in a timely manner. In 2013, the LSO made five attempts to obtain certain documents from the firm, which the firm failed to provide in a reasonable amount of time.
- **Proposed recommendation:** Set aside time to complete bookkeeping for your firm. Make an appointment in your calendar as a reminder to get the work done. If you can't keep up on your own, consider hiring a bookkeeper on contract or on a part-time basis.
- **Potential pitfall: Advertising your firm in a way that is not in accordance with the professional conduct of the region's law society.**
- **Possible fallout:** You may be fined by the law society and may need to spend more money remarketing your business.
- **Proposed recommendation:** Be honest, professional, and accurate when marketing your business. Do not oversell yourself or claim to be better than other legal professionals.

<sup>13</sup> SO 1994, c 11.

Direction To: The Manager

Name of bank: \_\_\_\_\_

(Name of chartered bank, provincial savings office, registered trust company, credit union or caisse populaire)

Branch: \_\_\_\_\_

Address: \_\_\_\_\_

Re: Account No. \_\_\_\_\_

Direction to Pay Interest to The Law Foundation of Ontario

The above account is  in my name

in the name of the firm with which I am associated

In accordance with Section 57 of the *Law Society Act*, I direct you, until further notice, to compute the amount earned by applying to the balance in the above account the rate of interest approved from time to time by the Trustees of The Law Foundation of Ontario. Please pay into an account held in your main office in Ontario in the name of The Law Foundation of Ontario amounts so calculated and give written notice to me at the address shown on the above account and to The Law Foundation of Ontario, 110 Spadina Avenue, Suite 800, Toronto, Ontario, M5V 2K4, when each such payment is made. This notice should show, as applicable as per the terms of the interest agreement between The Law Foundation of Ontario and your financial institution, the amount of the payment, the amounts of the daily/monthly balances, and the rates of interest used in computing the payment.

Dated: the day of \_\_\_\_\_, \_\_\_\_\_, 20\_\_\_\_\_

(Signed)

Licensee name: \_\_\_\_\_

Firm name: \_\_\_\_\_

Address: \_\_\_\_\_

cc: The Law Foundation of Ontario

FIGURE 1.5 Example letter of direction

Source: The Law Foundation of Ontario.

## PRACTICE REVIEW/AUDITS

All law firms are subject to law society compliance audits or reviews. In keeping with their mandates to govern the legal professions in the public interest, law societies use reviews to ensure the quality of legal services and advice given to the public. If the practice management capabilities of a licensee are deficient and could have an adverse effect on the quality of legal services offered to the public, the law society is required to take steps to provide guidance to the licensee. It will help correct deficiencies with practice management systems to avoid serious non-compliance, competence, or misconduct issues.

Audits can be either random or focused. A random practice review is proactive and preventive in nature and designed to ensure that licensees in private practice conduct their practices in an efficient, effective, and competent manner. Selection of licensees for a focused practice review is governed by a law society's by-laws or rules for regulating the conduct, capacity, and professional competence of licensees. Complaints from clients can trigger a review.

In conducting an audit, the auditor will:

- help law firms correct minor problems with record-keeping before they lead to serious issues of non-compliance and possible professional conduct issues;
- do an in-depth review of accounting records and a sample check of client files to ensure trust funds are being handled properly;
- answer any questions licensees have about trust accounting; and
- help licensees develop proper accounting systems, record-keeping practices, and trust fund handling procedures.

Once the review is completed, the file may be closed or suggestions may be made with a follow-up review to ensure compliance. Failure to meet the required standard of competence or to co-operate with the process can result in disciplinary action.

## CHAPTER SUMMARY

Whether you decide on a career as a licensee working alone or in association with other licensees, you need to have an understanding of record-keeping. Although you may not be directly involved in preparing bookkeeping entries and financial statements, you will be accountable to clients and must protect their interests. It is your responsibility to ensure that the firm you work with acts ethically and with integrity. Even when working in association with other licensees, a licensee often maintains their own trust account and is required to account for funds received in trust.

You will be required to submit annual reports to the law society and the law foundation and annual returns to the CRA. Having proper systems in place makes it easier to comply with all these obligations.

## KEY TERMS

affiliation, 5	limited liability partnership, 4
bookkeeper, 6	mixed, 10
bookkeeping, 6	monetary retainer, 9
Canada Revenue Agency (CRA), 7	multi-discipline practice (MDP), 5
chartered professional accountant (CPA), 6	partnership, 4
Federation of Law Societies of Canada, 2	pooled trust bank account, 10
general bank account, 9	posted, 10
general retainer, 9	professional corporation, 5
law foundations, 7	retainer, 8
law societies, 2	separate interest-bearing trust account, 11
licensees, 2	sole proprietorship, 4

## FURTHER READING

“Law Office Accounting in Alberta” (November 2017), online (pdf): *Law Society of Alberta* <[https://documents.lawsociety.ab.ca/wp-content/uploads/2017/06/14225753/TAB6\\_7\\_LawOffice\\_Accounting\\_in\\_AB1.pdf](https://documents.lawsociety.ab.ca/wp-content/uploads/2017/06/14225753/TAB6_7_LawOffice_Accounting_in_AB1.pdf)>.

Law Society of Ontario, *Bookkeeping Guide* (Toronto: LSO, 2022), online: <<https://lso.ca/lawyers/practice-supports-and-resources/topics/managing-money/bookkeeping>>.

“Revenue and Reporting” (3 February 2023), online: *The Law Foundation of Ontario* <<https://lawfoundation.on.ca/about-us/revenue-and-reporting>>.

“Sample Books and Records for Paralegals” (December 2015), online: *Law Society of Ontario* <<https://lso.ca/lawyers/practice-supports-and-resources/topics/managing-money/bookkeeping/sample-books-and-records-for-paralegals>>.

## REVIEW QUESTIONS

LO1 refers to Learning Outcome 1, listed at the beginning of the chapter. Check the margin of your book to see where LO1 is discussed in the chapter.

### True or False

- \_\_\_ 1. A separate interest-bearing trust account should be opened for each client. **(LO4)**
- \_\_\_ 2. A general retainer does not get deposited into the trust account. **(LO4)**
- \_\_\_ 3. It is a mandatory requirement for a legal professional to open and maintain a trust account. **(LO4)**
- \_\_\_ 4. Licensees may operate a legal practice with unlicensed professionals who provide other non-legal services. **(LO2)**
- \_\_\_ 5. Law societies regulate the form of business organization a licensee may choose. **(LO2)**
- \_\_\_ 6. Income taxes payable to the CRA in a partnership are paid by the partnership itself. **(LO2)**
- \_\_\_ 7. Understanding basic bookkeeping and accounting principles is useful only for the legal professional's reporting requirements to the law society. **(LO1)**
- \_\_\_ 8. Moneys received from a client for services not yet rendered should be deposited into the trust bank account. **(LO4)**
- \_\_\_ 9. A cheque received from a client as a retainer would be deposited in trust. **(LO5)**
- \_\_\_ 10. Hiring a bookkeeper or accountant to record transactions and prepare statements is a waste of money. **(LO4)**

### Short Answer

Give a full answer for each question.

1. What is the name and website address of the law society in your province or territory? **(LO1)**

Province/Territory	Name of Law Society	URL
British Columbia		
Alberta		
Saskatchewan		
Manitoba		
Ontario		
Quebec (Lawyers)		
Quebec (Notaries)		
New Brunswick		
Nova Scotia		
Prince Edward Island		
Newfoundland & Labrador		
Yukon		
Northwest Territories		
Nunavut		



2. What is the difference between the role played by a bookkeeper and that played by an accountant? **(LO2)**
3. What business structure is most likely to be used by a licensee opening an office and planning to work from home? **(LO2)**
4. Assume a firm has two bank accounts—a general bank account and a mixed trust account. Indicate whether the following transactions would involve a deposit or cheque and the bank account that would be used. **(LO4)**

Transaction	General Bank Account	Trust Bank Account
Licensee pays rent for the month	Cheque	
Licensee receives a retainer in the amount of \$1,000 from a new client, Jane Phillips		
Licensee invests \$5,000 into the firm		
Licensee pays court filing fees of \$150 on the Jane Phillips file		
Licensee pays telephone bill		
Licensee withdraws money for personal expenses		
Licensee prepares an invoice on the Jane Phillips file and writes a cheque in payment of invoice from the above retainer		

5. Justin Case received a retainer cheque for \$1,000 from Richard Jones and deposited the cheque in this trust account. He needed to issue a statement of claim the same day, so he wrote a cheque against the trust deposit for \$150. Unfortunately, a week later, the cheque for \$1,000 was returned by Richard's bank for insufficient funds and Justin's bank was charged a \$25 NSF fee against his trust account.
  - a. Show the transactions mentioned above in the ledger below. What is the balance in the client trust ledger for Richard Jones?

Richard Jones, Trust Ledger			
Description	Deposits	Cheques	Balance
Richard Jones, retainer			
Small Claims Court, filing fee			
NSF cheque returned by bank			
Service charge			
Deposit to cover overdraft			

- b. What steps should Justin Case take to rectify the situation?
6. What happens to interest earned on a mixed trust account? **(LO4)**
7. In what circumstances should a licensee maintain a separate interest-bearing trust for a client? **(LO4)**
8. Look up the law foundation for your province or territory online. What is its mandate? **(LO1)**

## PUT IT INTO PRACTICE

### Case Study: Susan Wright

Susan Wright, a recent graduate from a registered legal program, wishes to start her own law firm. She plans to have a small office at this time and does not intend to bring in any partners or associates.

1. What bank accounts do you anticipate she will require?
2. What is involved in opening the accounts? Where can they be opened? Provide some real-life examples in the city or town you live in.
3. On the website for the law society in your province or territory, find out what information is required for opening a trust account at a financial institution. Explain what information the bank needs to be aware of when opening a trust bank account for a law firm and how interest on the mixed trust account is paid.
4. Should Susan purchase legal software to help with her practice? Review some of the software companies shown below and select one you feel would be appropriate. Explain why you chose the one you did.
  - a. Abacus Law <<https://www.amicusattorney.com/abacuslaw>>
  - b. Clio <<https://www.clio.com/partnerships/bar-associations/lsa>>
  - c. CosmoLex <<https://www.cosmolex.ca>>
  - d. PCLaw <<https://pclawtimematters.ca>>
  - e. Soluno <<https://www.soluno.legal>>
  - f. uLaw <<https://www.ulaw.io>>
5. What form of business organization would be recommended?