

December 21, 2007

Dear Compliance Officer:

We are writing to remind you of recent changes affecting IOLTA accounts in California and to outline the process and timetable for implementing those changes.

As we indicated in our November 21, 2007, letter, the California legislature recently amended the statute governing Interest on Lawyers' Trust Accounts (IOLTA), effective January 1, 2008.¹ The amendments update the kinds of accounts in which IOLTA funds can be placed, allowing the use of sweep accounts that invest the funds overnight in conservative, high-yield bank products such as repurchase agreements backed by government securities or money market mutual funds invested in government securities.

Under the amendments, participation in IOLTA remains voluntary for financial institutions. Attorneys, however, may deposit client funds only in financial institutions that are "eligible," as defined, in part, by the statute's new interest rate comparability requirement:

"... if an eligible institution offers or makes investment products available to non-IOLTA customers, in order to remain an IOLTA eligible institution, it shall make those products available to IOLTA customers or pay an interest rate on the IOLTA deposit account that is comparable to the rate of return or the dividends generally paid on that investment product for similar customers meeting the same minimum balance and other requirements applicable to the investment product."

Because the amendments become effective January 1, 2008, we are notifying your Bank about the amendments and the process that the Legal Services Trust Fund Program of the State Bar will undertake in the weeks ahead to assist your bank in determining what, if any, changes in your IOLTA accounts will be needed. We are committed to working with you to make the implementation as smooth as possible for you and your IOLTA customers.

The Legal Services Trust Fund Program, as the administrator of the California IOLTA program, requires certain information to determine whether your bank already meets the rate comparability requirement or must adjust rates in order to obtain approval as an IOLTA-eligible financial institution. We are working, therefore, with each IOLTA-participating bank to ensure that California attorneys continue to be able to hold IOLTA accounts in their current financial institutions. This letter, with enclosures, outlines the following:

- Request for rate and fee information from your bank
- Process and timetable for implementation
- Approaches for achieving comparability
- Comparability status of financial institutions
- Pledge of intent to comply by March 1, 2008, or retroactively to that date

Request for information from your bank by January 31, 2008

In order to determine whether your bank is an eligible financial institution under the amended IOLTA statute, and to keep this process on schedule, we ask that Your Bank fill out the enclosed California IOLTA Rate Comparability Information Form. Please return the completed form, along with copies of relevant bank brochures or other account documents requested, to the Trust Fund Program in the enclosed envelope **no later than January 31**. We will review that information and advise your bank of any changes needed.

¹ Business and Professions Code §§6091.2, 6211, 6212, 6213.

Process and timetable for banks to implement the amended IOLTA statute

The Trust Fund Program will take a number of steps in the weeks ahead to assist you in determining what, if any, changes to your bank's IOLTA accounts will be needed to implement the amended IOLTA statute. We understand that the statute may require significant changes for some banks, and we will work with your bank to make the process proceed as efficiently as possible. **The enclosed timetable summarizes those steps and the deadlines necessary for your bank to achieve full compliance.**

We ask that you pay special attention to the **January 31 reply deadline** for the return of rate and fee information and the **March 1 compliance deadline** for aligning IOLTA rates with the comparability requirement of the amended IOLTA statute. You should contact the Trust Fund Program immediately if your bank anticipates that it cannot meet the enclosed timetable. In addition, we ask that each financial institution sign the enclosed Pledge of Intent and return it by January 31. The Pledge of Intent specifies that should a bank's eligibility and implementation process extend beyond the March 1 deadline, the financial institution will pay the comparable rate(s) (as defined by the IOLTA statute) retroactive to March 1. Any delay in implementation could jeopardize your bank's approval as an IOLTA-eligible financial institution.

The Trust Fund Program recognizes that some banks might be in compliance already with the interest rate comparability requirement. We will deem a financial institution in compliance if it provides documentation enabling the Trust Fund Program to certify that the rates or dividends the institution pays IOLTA are no less than the bank pays non-IOLTA customers when IOLTA accounts meet or exceed the same minimum balance and other eligibility qualifications. Otherwise, the bank will need to choose an approach for coming into compliance as outlined below.

Approaches for complying with the rate comparability requirement

Although the rate comparability requirement applies to all IOLTA accounts, the amended IOLTA statute affects most significantly the IOLTA accounts whose high balances and other characteristics qualify them for investment sweep accounts, premium checking accounts, or other high-rate accounts that your bank currently offers to its non-IOLTA customers holding comparable balances. Typically, those "high balance" accounts hold average balances of \$100,000 or more.

An IOLTA-eligible institution must pay comparable interest rates or dividends as required under Business and Professional Code 6212(b) and 6212(e) and may choose to do so in one of three ways:

- **Approach 1: Establish IOLTA accounts as comparable products** – Banks may comply by establishing IOLTA accounts as the highest-rate product(s) for which IOLTA accounts are eligible. As an example, if your bank's highest-rate IOLTA-eligible product is an overnight REPO sweep or money market mutual fund sweep account, then IOLTA accounts that meet the same minimum balance and other requirements could be moved into that product. Those IOLTA accounts would be assessed the same sweep fees and other fees allowable under the amended statute and implementing rules. The Trust Fund Program would take responsibility for obtaining executed sweep account forms by the lawyer or law firm. Smaller accounts not qualifying for the sweep rates might earn the bank's highest interest checking rates. If your bank does not have a business sweep account for which IOLTA is eligible, but offers tiered checking accounts to non-IOLTA customers for which IOLTA is eligible, the bank could apply those checking rates and tier structures to its IOLTA accounts.
- **Approach 2: Emulate the comparable product rate** – Instead of establishing IOLTA accounts as highest-rate products such as money market or other business sweep accounts, an institution simply can choose to pay the equivalent rates, less chargeable fees, if any, of those products on the IOLTA deposit accounts meeting the same minimum balance and other requirements. The bank will be deemed to be in compliance if it emulates the rates (less chargeable fees) of its highest-rate product or if the resulting blended net yield of the IOLTA portfolio, earning those

rates and paying those allowable fees, equals the blended net yield of an equivalent portfolio of non-IOLTA accounts meeting the same principal balance and other requirements.

- **Approach 3: Established Compliance Rate** – A financial institution may comply by adjusting the net yield on its IOLTA accounts to a rate determined by the Legal Services Trust Fund Commission, with the rate currently set at 68 percent of the Federal Funds Target Rate. An institution that chooses this approach will be deemed in compliance and will remain eligible as long as it maintains this relationship between IOLTA net yield and the Federal Funds Target Rate, as well as meeting other requirements of the amended IOLTA statute. This Established Compliance Rate may be adjusted once a year by the Trust Fund Program, upon 90 days' written notice to financial institutions participating in the IOLTA program.

In summary, the Trust Fund Program is committed to helping your institution comply with the changes in the IOLTA statute and has outlined a process and timetable to work together efficiently to achieve that goal. The Trust Fund Program has contracted with The Resource for Great Programs, Inc., for technical assistance in implementing these changes. The Resource for Great Programs is a national consulting firm that assists IOLTA programs and financial institutions in Florida, Michigan, Connecticut, Texas, and other states in implementing similar comparability changes.

If you are not the appropriate contact for IOLTA rate comparability implementation at your bank, please forward this letter and the enclosures to the appropriate bank representative(s).

The Legal Service Trust Fund Program, California lawyers, and financial institutions have been in partnership for more than 20 years. The Trust Fund Program distributes IOLTA funds to approximately 100 nonprofit organizations statewide that provide free legal services to help meet the basic civil legal needs each year of thousands of the most vulnerable Californians, including the elderly, children, and people with disabilities. We look forward to our continued partnership.

If you have any questions, please contact me at your earliest convenience.

Sincerely,

Stephanie L. Choy
Managing Director