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# The Future of IOLTA: Has the Death Knell Been Sounded for Mandatory IOLTA Programs?

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## THE FUTURE OF IOLTA: HAS THE DEATH KNELL BEEN SOUNDED FOR MANDATORY IOLTA PROGRAMS?

*“While the final nail has not been pounded into the IOLTA coffin, the next to the last one has.”<sup>1</sup>*

### I. INTRODUCTION

In Ohio,<sup>2</sup> a battered wife is being challenged by her ex-husband for custody of their son.<sup>3</sup> Due to the fact that she is indigent<sup>4</sup> and cannot afford an attorney, she must rely on legal aid services in her custody battle.<sup>5</sup> The scarcity of legal aid services<sup>6</sup> requires her to compete for legal services with a seventy-four year old gentlemen who was a recent target in an elaborate scam which bilked him of much of his pension, and an elderly woman being unfairly evicted from her apartment so it can be torn down to accommodate a new development.<sup>7</sup>

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<sup>1</sup> *IOLTA May Be Invalid - U.S. Supreme Court*, LAW. WLKY. U.S.A., June 29, 1998, at 2. (quoting Richard Samp, Washington Legal Foundation Chief Counsel, commenting on the United States Supreme Court’s recent ruling in *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925 (1998)).

<sup>2</sup> Ohio is a mandatory IOLTA state. OHIO REV. CODE ANN. § 4705.09(A)(2) (Banks-Baldwin 1998). “IOLTA” is an acronym for Interest on Lawyers’ Trust Accounts. BLACK’S LAW DICTIONARY 828 (6<sup>th</sup> ed. 1990) “In some states, lawyers turn over such interest to public service institutions.” *Id.* The majority of the interest earned on lawyers’ trust accounts is in turn used to fund legal services for the poor. *IOLTA May Be Invalid*, *supra* note 1, at 2. In Ohio, interest earned on lawyers trust accounts must be turned over to the State Treasurer. § 4705.09(B). The Treasurer in turn deposits the money into a legal aid fund. *Id.* For a look at how the legal aid fund was established, see § 120.52.

<sup>3</sup> This fictitious fact pattern is modeled after an example in Edward F. Hennessey, *Legal Services Program for the Poor is Still Alive*, BOSTON GLOBE, July 25, 1998, at A15.

<sup>4</sup> For the purposes of determining financial assistance to legal aid societies in Ohio, an “indigent” is defined as “a person or persons whose income is not greater than one hundred twenty-five per cent of the current poverty threshold established by the United States office of management and budget.” § 120.51(B).

<sup>5</sup> The Legal Services Corporation was created in 1974 under the Nixon Administration with the goal of assuring low income citizens across the country access to the legal system. Katherine Elrich, Note, *Equal Justice Under the Law (If You Can Afford It): Fifth Circuit Threatens Texas’ IOLTA Program*: *Washington Legal Found. v. Texas Equal Access to Justice Foundation*, 28 TEX. TECH L. REV. 887, 897 (1997). Currently, the Legal Services Corporation is a federally funded corporate entity that provides grants “to local poverty law groups” which in turn provide legal services to the poor. David A. Price, *Legal Services’ Stealth Funding*, INV. BUS. DAILY, October 15, 1996 at A1. Legal Services Corporation also relies heavily on monies received from IOLTA programs. *Id.* For more information on the Legal Services Corporation, visit their web site at *Legal Services Corporation* (visited Oct. 1, 1998) <[http://www.cuberus.ca/~ppp/profiles/legal\\_se.htm](http://www.cuberus.ca/~ppp/profiles/legal_se.htm)>.

<sup>6</sup> See, e.g., Price, *supra* note 5, at A1 (stating that in 1996, Congress cut funding for the Legal Services Corporation by thirty percent).

<sup>7</sup> These facts are fictitious. The reality lies in the fact that many of Legal Services Corporation’s cases involve evictions and child custody cases. Price, *supra* note 5, at A1. In 1995 alone, over 500,000 of Legal Services Corp’s cases involved family law. *Id.* Over

The United States Constitution guarantees a criminal defendant the right to counsel.<sup>8</sup> However, it does not afford a civil litigant similar protection.<sup>9</sup> The troubled individuals previously discussed must either rely on legal aid services or face the daunting task of *pro se*<sup>10</sup> representation.<sup>11</sup>

Legal aid services receive much of their funding from programs such as Interest on Lawyers' Trust Accounts (IOLTA).<sup>12</sup> The main purpose of an IOLTA program is to permit the interest earned on pooled client trust accounts to be used to fund legal

250,000 cases in 1995 involved housing. *Id.*

<sup>8</sup> The Sixth Amendment to the United States Constitution states:

In all *criminal* prosecutions, the accused shall enjoy the right to a speedy and public trial, by an impartial jury of the State and district wherein the crime shall have been committed, which district shall have been previously ascertained by law, and to be informed of the nature and cause of the accusation; to be confronted with the witnesses against him; to have compulsory process for obtaining Witnesses in his favor, *and to have the Assistance of Counsel for his defence.*

U.S. Const. amend. VI. (emphasis added); *cf.* M.L.B. v. S.L.K., 117 S. Ct. 555 (1996). The United States Supreme Court stated "[T]he right to counsel at state expense . . . is less encompassing. A State must provide trial counsel for an indigent defendant charged with a felony, but that right does not extend to nonfelony trials if no term of imprisonment is actually imposed." *Id.* at 562 (1996) (citations omitted).

<sup>9</sup> See GERALD GUNTHER & KATHLEEN M. SULLIVAN, CONSTITUTIONAL LAW 899-901 (13<sup>th</sup> ed. 1997). While a State may not be required to provide an attorney for a civil litigant, it may not always deny access to its courts to a civil litigant solely on his or her inability to pay litigation costs. *See, e.g.*, M.L.B. v. S.L.J., 117 S. Ct. 555 (1996) (holding that a state may not deny access to courts, solely on a parties inability to pay, in parental termination cases); *Boddie v. Connecticut*, 401 U.S. 371 (1971) (holding that a state cannot deny, solely on a parties inability to pay, access to its courts for individuals seeking to terminate their marriage); *Little v. Streater*, 452 U.S. 1 (1981) (holding that an indigent defendant in a paternity action is entitled to state sponsored blood grouping tests). *But cf.* *United States v. Kras*, 409 U.S. 434 (1973) (upholding fifty dollar filing fee in a voluntary bankruptcy proceeding); *Orstein v. Schwab*, 410 U.S. 656 (1973) (upholding twenty-five dollar fee for a review of a denial of welfare benefits).

<sup>10</sup> "Pro se" can be defined as "[f]or one's own behalf; in person. Appearing for oneself, as in the case of one who does not retain a lawyer and appears for himself in court." BLACK'S LAW DICTIONARY 1221 (6<sup>th</sup> ed. 1990).

<sup>11</sup> Former Chief Justice of the Massachusetts Supreme Judicial Court Edward Hennessey explains "As a former judge, I saw firsthand the effects of the legal services shortages. Litigants who come to court pro se . . . are at a significant disadvantage in the courtroom, and it is extremely difficult for the judge in these cases to ensure that justice is served." Hennessey, *supra* note 3, at A15. Another possibility is "pro bono" representation. "Pro bono" can be defined as "[f]or the good; used to describe work or services (e.g. legal services) done or performed free of charge." BLACK'S LAW DICTIONARY 1221 (6<sup>th</sup> ed. 1990). The American Bar Association's Model Rules of Professional Conduct states that "[a] lawyer should aspire to render at least (50) hours of pro bono publico services per year." MODEL RULES OF PROFESSIONAL CONDUCT Rule 6.1 (1997) (emphasis added).

<sup>12</sup> *See, e.g., IOLTA May Be Invalid, supra* note 1, at 2.

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 services for the financially disadvantaged.<sup>13</sup> Since their inception, IOLTAs have been highly controversial and under constitutional attack.<sup>14</sup> These attacks have been largely unsuccessful,<sup>15</sup> until a recent United States Supreme Court decision placed the constitutionality of IOLTA programs in serious doubt.<sup>16</sup>

This comment seeks to outline the history of IOLTA, its current status, and its probable future in light of recent court decisions. First, the comment considers the history of IOLTA programs in both the United States and in Ohio.<sup>17</sup> Second, it examines the primary types of constitutional challenges endured by IOLTA programs.<sup>18</sup> Third, this comment focuses on the unlikely continued viability of IOLTA programs, in light of recent court decisions.<sup>19</sup> Finally, this comment concludes with the proposition that mandatory IOLTA programs are on the verge of being declared unconstitutional and that states will need to consider alternative sources of money to fill the funding void left in the wake of IOLTA's apparent demise.<sup>20</sup>

## II. BACKGROUND

### A. *Origination of IOLTA in the United States*

While IOLTAs are relatively new in the United States, the concept has been widely implemented around the world.<sup>21</sup> In considering the history of IOLTA in the United States, one must first consider the underlying need for such a program. Both the

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<sup>13</sup> *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1928 (1998). However, this is not the only worthwhile cause funded by IOLTA programs. *See Cone v. State Bar of Florida*, 819 F.2d 1002, 1004 (11<sup>th</sup> Cir. 1987) (stating that funds from Florida's IOTA program were used to fund law student scholarships).

<sup>14</sup> *See generally* Kevin H. Douglas, Note, *IOLTAS Unmasked: Legal Aid Programs' Funding Results in Taking of Client's Property*, 50 VAND. L. REV. 1297, 1333 (1997) (accusing IOLTA programs of "quietly confiscating property from a dispersed political minority").

<sup>15</sup> *See, e.g.,* *Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962 (1<sup>st</sup> Cir. 1993); *Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987); *In re Interest on Trust Accounts*, 356 So. 2d 799 (Fla. 1978).

<sup>16</sup> *See Phillips*, 118 S. Ct. at 1925 (holding that under Texas law, interest generated by IOLTA accounts constituted private property for the purpose of Takings Clause analysis). The Fifth Amendment to the United States Constitution provides: "No person . . . shall be deprived of life, liberty, or property, without due process of law; nor shall *private property* be taken for public use, without just compensation." U.S. CONST. amend. V. (emphasis added).

<sup>17</sup> *Infra* Part II.A-B.

<sup>18</sup> *Infra* Part III.A-B.

<sup>19</sup> *Infra* Part IV.A-D.

<sup>20</sup> *Infra* Part V.

<sup>21</sup> As of 1978, interest was being paid on lawyers' trust accounts in the following countries: South Africa, Rhodesia, Australia, and Canada. *In re Interest on Trust Accounts*, 356 So. 2d 799, 803, n.25 (Fla. 1978). In countries such as South Africa, participation in the IOLTA program is optional; while in others such as Australia and Canada, participation is mandatory. *Id.* at n.27. In the vast majority of these countries, IOLTA programs have been largely successful. *Id.*

ABA<sup>22</sup> Model Code of Professional Responsibility<sup>23</sup> and the ABA Model Rules of Professional Conduct<sup>24</sup> prohibit the commingling of a client's funds with those of an attorney.<sup>25</sup> As such, attorneys have traditionally set up pooled client trust accounts, in which the client's money is placed for the duration of the representation.<sup>26</sup> Prior to

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<sup>22</sup> ABA is an acronym for American Bar Association. The American Bar Association was founded in New York in 1878 by over 100 lawyers representing twenty-one states. *See ABA Media Relations and Public Affairs, ABA History* (visited September 19, 1998) <<http://www.abanet.org/media/overview/phistory.html>>. The American Bar Association's stated mission is "to be the national representative of the legal profession, serving the public and the profession by promoting justice, professional excellence and respect for the law." *Id.*

<sup>23</sup> The Model Code of Professional Responsibility was adopted by the American Bar Association in 1969. THOMAS D. MORGAN & RONALD D. ROTUNDA, PROFESSIONAL RESPONSIBILITY 12 (6<sup>th</sup> ed. 1995). The Model Code of Professional Responsibility contains both 'Disciplinary Rules' and 'Ethical Considerations.' *Id.* Only a violation of a 'Disciplinary Rule' will subject the violating attorney to discipline, up to disbarment. *Id.* It is important to note that neither the Model Code nor the Model Rules are legally binding until adopted by a state's supreme court. *Id.* The Model Code was subsequently adopted by almost every state supreme court. *Id.* The Supreme Court of Ohio adopted the Model Code of Professional Responsibility on October 5, 1970 and continues to use it today. OH. ST. GOVT. BAR RULE 4. For a look at conduct in the legal profession prior to the adoption of the Model Code of Professional Responsibility, see Vern Countryman, *The Scope of Lawyer's Professional Responsibility*, 26 OHIO ST. L.J. 66 (1965).

<sup>24</sup> The Model Rules of Professional Conduct were adopted by the American Bar Association in 1983. MORGAN & ROTUNDA, *supra* note 23, at 12. The Model Rules of Professional Conduct contain both 'Rules' and 'Comments.' *Id.* Violation of a 'Rule' may subject an attorney to discipline. *Id.* Similarly, the 'Comments' are considered to have "authoritative status." *Id.* As of 1995, the Model Rules have been adopted in over thirty-five states. *Id.*

<sup>25</sup> MODEL CODE OF PROFESSIONAL RESPONSIBILITY DR 9-102 (1983). The Rule states:  
 (A) All funds of clients paid to a lawyer or law firm, other than advances for costs and expenses, shall be deposited in one or more identifiable bank accounts maintained in the state in which the law office is situated and no funds belonging to the lawyer or law firm shall be deposited therein . . . .  
*Id.* For a look at how the rule has been applied in Ohio, see Columbus Bar Ass'n. v. Kostelac, 687 N.E.2d 408 (Ohio 1997) (holding that an attorney is subject to discipline for commingling his client's funds with his own, even where the client is not prejudiced); Office of Disciplinary Counsel v. Shaw, 472 N.E.2d 1075 (Ohio 1984) (stating that the misappropriation of a client's funds is grounds for indefinite suspension). Similarly, the ABA Model Rules of Professional Conduct Rule 1.15 states:

(a) A lawyer shall hold property of clients or third persons that is in a lawyer's possession in connection with a representation separate from the lawyer's own property . . . complete records of such account funds shall be kept by the lawyer and shall be preserved for a period of [five years] after termination of the representation.

MODEL RULES OF PROFESSIONAL CONDUCT Rule 1.15(a) (1983).

<sup>26</sup> *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1928 (1998). This was the preferred method of holding client's funds, especially where the amount being held for an individual client was relatively small, due to the administrative inefficiencies and separate bank charges associated with maintaining separate accounts for each client. *Id.* Of course, when a lawyer held a "large sum in trust for his client, such funds were generally placed in an

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1982, these types of accounts were non-interest bearing.<sup>27</sup> Thus, the main beneficiaries of this type of arrangement were the financial institutions where the client's money was deposited.<sup>28</sup>

In 1982, Congress passed the Consumer Checking Account Equity Act.<sup>29</sup> The Act permitted interest to be paid on certain types of "available-on-demand" accounts,<sup>30</sup> while restricting ownership in the accounts to a select minority.<sup>31</sup> Specifically, the statute authorized nonprofit charitable organizations to benefit from such accounts.<sup>32</sup> Thus, a state could circumvent the restrictions by making a nonprofit charitable organization the sole recipient of the interest earned on the trust accounts.<sup>33</sup>

Florida became the first state to take advantage of the change in banking laws by implementing an IOTA<sup>34</sup> program through judicial decision<sup>35</sup> in 1981.<sup>36</sup> Other states

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interest-bearing savings account because the interest generated outweighed the inconvenience caused by the lack of check-writing capabilities." *Id.*

<sup>27</sup> Before 1982, federal law prohibited banks from paying interest on demand accounts. 12 U.S.C.A § 1464 (West Supp. 1998) (amended 1982). Specifically, 12 U.S.C.A § 1464(b)(1)(B) stated: "[a] Federal savings association may not— (i) pay interest on a demand account." *Id.*

<sup>28</sup> *Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987). The court stated that the banks were "treated to 'free' use of trust account deposits." *Id.* at 1005.

<sup>29</sup> 12 U.S.C. § 1832 (1987). Specifically, 12 U.S.C. § 1832(a)(1) reads: "Notwithstanding any other provisions of law but subject to paragraph (2), a depository institution is authorized to permit the owner of a deposit or account on which interest or dividends are paid to make withdrawals by negotiable or transferable instruments for the purpose of making transfers to third parties." *Id.*

<sup>30</sup> These accounts are also known as Negotiable Order of Withdrawal (NOW) accounts. *See Cone*, 819 F.2d at 1005.

<sup>31</sup> *See* 12 U.S.C. § 1832(a)(2) (1987) stating:

Paragraph (1) shall apply only with respect to deposits or accounts which consist solely of funds in which the entire beneficial interest is held by one or more individuals or by an organization which is operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes and which is not operated for profit . . . .

*Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *Cone*, 819 F.2d at 1006. In *Cone*, the State of Florida had set up a system where the Florida Bar Foundation was the sole recipient of all interest earned on lawyer trust accounts. *Id.* at 1004. The Foundation would then "allot the funds to legal aid organizations, law student scholarships, and other charitable purposes." *Id.*

<sup>34</sup> IOTA and IOLTA are in essence interchangeable. IOTA is an acronym for Interest on Trust Accounts. For ease of reading, the acronym IOLTA will be used throughout this comment.

<sup>35</sup> *In re Interest on Trust Accounts*, 402 So. 2d 389, 396 (Fla. 1981).

<sup>36</sup> Note that the act authorizing such action, the Consumer Checking Account Equity Act, did not become law until 1982. 12 U.S.C. § 1832 (1982). Even though Florida did not establish an IOLTA program until 1981, the concept had been considered by the State of Florida as early as 1971. *In re Interest on Trust Accounts*, 356 So. 2d at 800. For an interesting discussion on how the Internal Revenue Service helped shape the way the nation's first

soon followed suit,<sup>37</sup> some by judicial decision<sup>38</sup> and others through legislative enactment.<sup>39</sup> Additionally, some states have chosen to make participation in IOLTA programs mandatory,<sup>40</sup> while others have made participation optional.<sup>41</sup> Currently, all fifty states and the District of Columbia have some form of IOLTA program.<sup>42</sup>

### B. The Birth of IOLTA in Ohio

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IOLTA program was implemented, see Kristin A. Dulong, Note, *Exploring the Fifth Dimension: IOLTA, Professional Responsibility, and the Takings Clause*, 31 SUFFOLK U.L. REV. 91 (1997).

<sup>37</sup> Other states that implemented early IOLTA programs include Minnesota, New Hampshire, Utah, Arkansas, Massachusetts, and California. *Cone*, 819 F.2d at 1006.

<sup>38</sup> Whether a state will implement an IOLTA program through judicial decision or legislative enactment depends upon “which government branch the state constitution holds responsible for regulating the state’s legal profession.” Terence E. Doherty, *The Constitutionality of IOLTA Accounts*, 19 WHITTIER L. REV. 487, 490 (1998).

<sup>39</sup> California and Maryland are examples of states which have adopted IOLTA programs through legislative enactment. For more information on these programs, see Betsy Borden Johnson, Comment, *‘With Liberty and Justice For All’ IOLTA in Texas - The Texas Equal Access to Justice System*, 37 BAYLOR L. REV. 725 (1985).

In contrast, Texas serves as an example of a state that was forced to create a voluntary IOLTA program through judicial decision after an attempt to create a mandatory program failed in the legislature. See Elrich, *supra* note 5, at 895 (citing *In re Interest on Trust Accounts*, 402 So. 2d 389, 396 (Fla. 1981)). In December of 1981, the Texas Bar created a committee to study the feasibility of implementing an IOLTA program. *Id.* (citing Johnson, *supra*, at 736). The committee recommended establishing a mandatory IOLTA program and, in 1983, the Texas Bar subsequently drafted legislation that was presented to the Texas legislature. *Id.* The proposed statute failed in the legislature and the Texas Bar was forced to settle for a voluntary IOLTA program later adopted by the Texas Supreme Court. *Id.*

<sup>40</sup> Currently, twenty-six states have mandatory IOLTA programs. Brennan J. Torregrossa, Note, *Washington Legal Foundation v. Texas Equal Access to Justice Foundation: Is there an IOTA of Property Interest in IOLTA?*, 42 VILL. L. REV. 189, 192 (1997). Examples of states that have made participation in an IOLTA program mandatory include: Arizona, California, Iowa, Minnesota, Washington and Wisconsin. Phillip F. Downey, Comment, *Attorney’s Trust Accounts: The Bar’s Role in the Preservation of Client Property*, 49 OHIO ST. L.J. 275, n.32 (1988) (citation omitted). Participation in Ohio’s IOLTA program is also mandatory. See *infra* Part II.B.

<sup>41</sup> The first IOLTA program in the country was optional. Elrich, *supra* note 5, at 894. In 1988, because of the success in generating interest experienced by IOLTA programs in “mandatory” IOLTA states, the American Bar Association recommended that all states convert to a mandatory program. Doherty, *supra* note 38, at 491. Currently, twenty-four states have some form of optional IOLTA program. *Id.* For more information on the differences between mandatory and voluntary IOLTA programs, see generally Torregrossa, *supra* note 40.

<sup>42</sup> Indiana was the last state to implement an IOLTA program. David J. Remondini, *IOLTA Arrives in Indiana: Trial Judges To Play Key Role In Pro Bono Plan*, 41 RES GESTAE 9 (Indiana Bar Association, Feb. 1998). Indiana’s voluntary IOLTA program was formally adopted by the Indiana Supreme Court on October 22, 1997. *Id.* For more on the history of IOLTA programs in the United States, see generally Dulong, *supra* note 36; Douglas, *supra* note 14.

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Ohio first considered the idea of establishing an Interest on Lawyer's Trust Account program in the early 1980's.<sup>43</sup> It appears that Ohio's initial consideration of IOLTA was precipitated by two factors. First, recent changes in the nation's banking laws made it permissible to establish interest bearing "available on demand accounts."<sup>44</sup> For the first time, the payment of interest was permitted on certain types of "available-on-demand" accounts,<sup>45</sup> if they were held by a particular type of individual or organization.<sup>46</sup> The second precipitating factor was that other states<sup>47</sup> had implemented similar programs and were utilizing the earned interest to fund legal services for the disadvantaged.<sup>48</sup>

Combined, these factors prompted the Ohio State Bar Association<sup>49</sup> to form a committee to study the feasibility of an IOLTA program.<sup>50</sup> In 1983, a majority of the committee<sup>51</sup> not only recommended that a mandatory IOLTA program be established,<sup>52</sup>

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<sup>43</sup> Walter M. Lawson, *Condensed Report of the Committee to Study Interest on Lawyers Trust Accounts (IOLTA)*, 56 OHIO ST. B. ASS'N. REP. 1510, 1510 (1983).

<sup>44</sup> 12 U.S.C. § 1832 (1987). For a discussion of these code provisions, see *supra* notes 29-31 and accompanying text.

<sup>45</sup> 12 U.S.C. § 1832.

<sup>46</sup> *Id.* at (a)(2).

<sup>47</sup> When Ohio was first considering establishing an IOLTA program, fifteen states had already implemented some form of IOLTA, and two states had rejected the concept. Lawson, *supra* note 43, at 1514. Georgia and West Virginia were the two states who initially rejected the IOLTA concept. *Id.* However, by the time the Ohio State Bar Association recommended the implementation of IOLTA, both states had begun to reconsider the program. *Id.*

<sup>48</sup> See, e.g., *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1928 (1998); *Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987).

<sup>49</sup> The Ohio State Bar Association was founded in 1880. *OSBA Public Relations, Info on OSBA* (visited October 2, 1998) <[http://www.ohiobar.org/info/index\\_right.html](http://www.ohiobar.org/info/index_right.html)>. It is a voluntary professional organization comprised of nearly seventy-five percent of Ohio's lawyers and judges. *Id.*

<sup>50</sup> The Committee to Study Interest on Lawyers Trust Accounts was formed in 1982 by the Ohio State Bar Association. Lawson, *supra* note 43, at 1514. As the name states, the report is the condensed version of the full report issued by the committee. *Id.* For a copy of the full report, contact the Ohio State Bar Association, 33 W. 11<sup>th</sup> Avenue, Columbus, Ohio 43201.

<sup>51</sup> The final vote on the committee's recommendation to implement a mandatory IOLTA program in Ohio was eleven to one. Lawson, *supra* note 43, at 1535. The lone dissenter, Mr. Keith McNamara, not only felt that a mandatory IOLTA would unduly burden the state's financial institutions, but he also viewed IOLTA as unethical and unconstitutional. *Id.* Mr. McNamara's argument that IOLTA's would be unduly burdensome on Ohio's financial institutions was grounded in the fact that banks did not at the time have the software required to manage the numerous IOLTA accounts that would be required under a mandatory program. *Id.* at 1539. McNamara also viewed the manual administration of such accounts to be cost prohibitive. *Id.* On constitutional grounds, a debate was raging across the nation concerning whether or not a client had a property interest in the interest being earned on money being held in an IOLTA. *Id.* at 1536-37. McNamara found the argument that the client has no property interest in these monies to be illogical and unfounded in law. *Id.* at 1537.



but they also devised a basic framework of how to structure the IOLTA.<sup>53</sup> One of the key provisions in the proposed IOLTA structure stated that “IOLTA accounts are reserved exclusively for deposits that are either nominal in amount or are to be held for only a short time, or both.”<sup>54</sup>

Ohio’s IOLTA program was officially established by legislative enactment in 1985.<sup>55</sup> Key provisions in the Ohio State Bar Association’s report<sup>56</sup> were incorporated into the statute. For instance, the statute mandated that attorneys who accept clients’ funds in trust that are nominal in nature<sup>57</sup> or to be held for a short duration,<sup>58</sup> must place the funds in an IOLTA account.<sup>59</sup> The statute further mandates that interest earned on these accounts be deposited into a legal aid fund<sup>60</sup> by the Treasurer of the State of

<sup>52</sup> Lawson, *supra* note 43, at 1524. One of the main reasons the committee determined IOLTA worthy of implementation in Ohio was the fact that it was estimated that such a program would generate an estimated net annual income of three million dollars. *Id.* at 1510. In discussing why the committee chose to recommend that participation in the program be mandatory, the committee stated:

The Committee chose to recommend a mandatory plan in order to obtain maximum yield for the projects and programs to benefit from it. At the same time, the Committee was careful to carve out exceptions for smaller accounts in which interest earned would be unlikely to cover service charges, and when suitable interest-bearing accounts are not available.

*Id.* at 1524.

<sup>53</sup> Specifically, the Committee recommended that the IOLTA program be structured to “[t]ake into account ethical considerations and the practical aspects of maintaining trust accounts; to meet possible constitutional objections; to avoid unfavorable tax treatment; to provide a broad range of projects and programs to benefit from the plan; and to . . . make the plan acceptable to the general bar and public.” *Id.* at 1510.

<sup>54</sup> Lawson, *supra* note 43, at 1525. This provision is essentially codified in OHIO REV. CODE ANN. § 4705.09(A)(2)(a) (Banks-Baldwin 1998); *see infra* note 59. “What constitutes ‘nominal’ or ‘short-term’ is left to the attorney’s sound judgement, with the provision that charges of misconduct cannot be predicated on the exercise of such judgement.” Lawson, *supra* note 43, at 1525. However, the Committee inferred that deposits of one thousand dollars or less for periods of thirty days or less would satisfy both the nominal and short-term requirements. *Id.*

<sup>55</sup> OHIO REV. CODE § 4705.09 (Banks-Baldwin 1998) (amended 1984, *effective* 1985).

<sup>56</sup> *See* Lawson, *supra* note 43, at 1525.

<sup>57</sup> Funds that are more than nominal in nature are exempt from the requirements of § 4705.09; *see supra* note 52.

<sup>58</sup> Lawson, *supra* note 43, at 1525. For a discussion of what constitutes a short duration, *see supra* note 54.

<sup>59</sup> § 4705.09(A)(2)(a). The statute states in pertinent part: “Each attorney who receives funds belonging to a client shall . . . deposit all client funds held that are nominal in amount or are to be held by the attorney for a short period of time.” *Id.* Additionally, the statute requires that “each account established . . . shall be in the name of the attorney, firm, or association that established or is maintaining it and shall be identified as an IOLTA or an interest on lawyer’s trust account.” § 4705.09(A)(1).

<sup>60</sup> *Id.* For a look at how the legal aid fund was established, *see* OHIO REV. CODE ANN. § 120.52 (Banks-Baldwin 1995).

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Ohio.<sup>61</sup> Legal aid funds are in turn used to fund legal aid societies.<sup>62</sup>

The legislature also provided for the Ohio Supreme Court to have the power to adopt and enforce rules pertaining to the use and enforcement of IOLTAs.<sup>63</sup> For the most part, the Ohio statute<sup>64</sup> has remained unchanged in the fourteen years since its inception.<sup>65</sup>

### III. HISTORICAL CONSTITUTIONAL ATTACKS ON IOLTA

Almost as quickly as IOLTA programs were being established around the country,<sup>66</sup> they were being challenged.<sup>67</sup> Historically, IOLTA programs have been challenged on

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<sup>61</sup> OHIO REV. CODE ANN. § 4705.09(B). The statute states in pertinent part:

All interest earned on funds deposited in an interest-bearing trust account . . . shall be transmitted to the treasurer of state . . . No part of the interest earned on funds deposited in an interest-bearing trust account . . . shall be paid to, or inure to the benefit of, the attorney, the attorney's law firm or legal professional association, the client or other person who owns or has a beneficial ownership of the funds deposited, or any other person other than in accordance with this section, section 4705.10, and sections 120.51 to 120.55 of the Revised Code.

*Id.* Section 4705.10 pertains to the administration of IOLTAs. Sections 120.51 to 120.55 of the Ohio Revised Code pertain to legal aid funds.

<sup>62</sup> A Legal Aid Society is a:

[N]onprofit corporation that satisfies all of the following:

(1) It is chartered to provide general legal services to the poor, it is incorporated and operated exclusively in this state, its primary purpose or function is to provide civil legal services, without charge, to indigents, and in addition to providing civil legal services to indigents, it may provide legal training or legal technical assistance to other legal aid societies in this state.

(2) It has a board of trustees, a majority of its board of trustees are attorneys, and at least one-third of its board of trustees, when selected, are eligible to receive legal services from the legal aid society.

(3) it receives funding from the legal services corporation or otherwise provides civil legal services to indigents.

OHIO REV. CODE ANN. §§ 120.51(A)(1)-(3) (Banks-Baldwin 1998). For a better understanding of what the term "indigent" means under the statute, see *supra* note 4. For more information on the Legal Services Corporation, see *supra* note 5.

<sup>63</sup> See OHIO REV. CODE ANN. § 4705.09(D). The Ohio State Supreme Court also governs the conduct of attorneys generally. See generally OHIO GOV'T BAR RULES 4-5 (Banks-Baldwin 1998) (establishing a Board of Commissioners on Grievances and Discipline of the Supreme Court); Stanley A. Samad, *Ohio Revised Rules for the Government of the Judiciary and the Bar: A Critique*, 13 CAP. U. L. REV. 25 (1983).

<sup>64</sup> § 4705.09.

<sup>65</sup> Minor textual revisions were made in a 1995 amendment.

<sup>66</sup> Florida established the first IOLTA program in 1981. *In re Interest on Trust Accounts*, 402 So. 2d 389, 389 (Fla. 1981). By 1983, fifteen states had adopted some form of an IOLTA program. See Lawson, *supra* note 43, at 1514.

<sup>67</sup> See W. Frank Newton and James W. Paulson, *Constitutional Challenges to IOLTA Revisited*, 101 DICK. L. REV. 549 (1997) (summarizing some constitutional challenges to IOLTA programs); see, e.g., *In re Minnesota State Bar Ass'n*, 332 N.W.2d 151 (Minn. 1982); *In re New*

two different constitutional grounds, namely under the First and Fifth Amendments to the United States Constitution. These challenges will be examined individually.

#### A. IOLTA and the First Amendment

In the past, IOLTA programs have been challenged as unconstitutional on the basis that they violate the First Amendment<sup>68</sup> to the United States Constitution.<sup>69</sup>

Challenges to IOLTA programs on First Amendment grounds can be segregated into two distinct groupings. The first involves First Amendment challenges to “voluntary”<sup>70</sup> IOLTA programs. Such challenges are virtually nonexistent.<sup>71</sup>

First Amendment<sup>72</sup> challenges to IOLTA programs that compel<sup>73</sup> participation constitute the second grouping.<sup>74</sup> Namely, the challengers<sup>75</sup> have asserted that the states’ use of interest earned on IOLTAs forces them to support ideological or political

Hampshire Bar Ass’n, 453 A.2d 1258 (N.H. 1982); *In re Interest on Lawyer’s Trust Accounts*, 672 P.2d 406 (Utah 1983); *In re Interest on Lawyer’s Trust Accounts*, 675 S.W.2d 355 (Ark. 1984); *In re Massachusetts Bar Ass’n*, 478 N.E.2d 715 (Mass. 1985); *Caroll v. State Bar of Cal.*, 213 Cal. Rptr. 305 (1985); *Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987).

<sup>68</sup> The First Amendment to the United States Constitution states “Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the Government for a redress of grievances.” U.S. CONST. amend. I. The First Amendment is made applicable to the several states by incorporation. *See, e.g., Palko v. Connecticut*, 302 U.S. 319 (1937).

<sup>69</sup> *See, e.g., Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962 (1<sup>st</sup> Cir. 1993); *Washington Legal Found. v. Texas Access to Justice Found.*, 94 F.3d 996 (5<sup>th</sup> Cir. 1996), *aff’d in part by Phillips v. Washington Legal Found.*, 118 S. Ct. 1925 (1998).

<sup>70</sup> States that have a “voluntary” IOLTA program usually permit the attorney to choose whether or not to participate in the program, whereas the client has little, if any, choice in the matter. *Washington Legal Found. v. Texas Access to Justice Found.* 94 F.3d 996, 998 (5<sup>th</sup> Cir. 1996).

<sup>71</sup> This is due to the fact that the First Amendment argument is premised on the proposition that participants are being forced to fund legal services they find to be offensive. *See Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962, 976 (1<sup>st</sup> Cir. 1993). However, if participation in an IOLTA program is voluntary, one can hardly claim that they are being forced. *But see Washington Legal Found. v. Texas Access to Justice Found.*, 94 F.3d 996, 998 (5<sup>th</sup> Cir. 1996) (stating that states with voluntary IOLTA programs usually leave the question of whether to participate in an IOLTA for the attorney).

<sup>72</sup> U.S. CONST. amend. I.

<sup>73</sup> States that have a “mandatory” IOLTA program mandate attorney participation. *See, e.g., OHIO REV. CODE ANN. § 4705.09(A)(2)(a)*; *see also Torregrossa, supra* note 40, at 192.

<sup>74</sup> *See Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962, 977 (1<sup>st</sup> Cir. 1993).

<sup>75</sup> Challengers include organizations such as the Washington Legal Foundation. *Washington Legal*, 993 F.2d at 962. The Washington Legal Foundation is a national, non-profit, tax-exempt public foundation. *Washington Legal Foundation’s - How to Support*, <<http://www.wlf.org/howtosup.htm>>. Founded in 1977, the Washington Legal Foundation’s only goal is “to defend and promote the principles of free enterprise and individual rights.” *Washington Legal Foundation’s Missions and Goal*, <<http://www.wlf.org/mission.htm>>.

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organizations they find to be offensive and in violation of both the right to free speech and the right to freedom of association under the First Amendment.<sup>76</sup> In essence, the argument proceeds that IOLTAs compel speech by requiring the client to financially support views to which the client is diametrically opposed. In the past, the United States Supreme Court has ruled that compelling financial support for private organizations “implicates First Amendment rights when the funds were used to subsidize ideological or political activities.”<sup>77</sup> Despite this, First Amendment challenges to IOLTA programs have been largely unsuccessful.<sup>78</sup>

In *Washington Legal Foundation v. Massachusetts Bar Foundation*,<sup>79</sup> appellants in a mandatory IOLTA program<sup>80</sup> claimed that their compelled participation<sup>81</sup> in the funding of ideological and political activities<sup>82</sup> violated their First Amendment<sup>83</sup> rights to freedom of speech and freedom of association.<sup>84</sup>

The district court granted the Massachusetts Bar Foundation’s motion to dismiss.<sup>85</sup>

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<sup>76</sup> See U.S. CONST. amend. I.

<sup>77</sup> *Washington Legal*, 993 F.2d at 977 (citing *Keller v. State Bar of Cal.*, 496 U.S. 1 (1990)); *Lehnert v. Ferris Faculty Ass’n*, 500 U.S. 507 (1991); *AFL-CIO v. Hudson*, 475 U.S. 292 (1986); *Ellis v. Railway Clerks*, 466 U.S. 435 (1984); *Abood v. Detroit Bd. of Educ.*, 431 U.S. 209 (1977); *Railway Clerks v. Allen*, 373 U.S. 113 (1963).

<sup>78</sup> See, e.g., *Washington Legal*, 993 F.2d 962 (involving a First Amendment challenge to Massachusetts “mandatory” IOLTA program); *Washington Legal Found. v. Texas Access to Justice Found.*, 94 F.3d 996 (5<sup>th</sup> Cir. 1996) (involving a First Amendment challenge to the Texas’ “mandatory” IOLTA program). *But cf.* *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925 (1998) (finding a property interest in interest earned by IOLTAs). For more information on the Court’s decision in *Phillips*, see *infra* Part IV.B.

<sup>79</sup> 993 F.2d 962 (1<sup>st</sup> Cir. 1993).

<sup>80</sup> Massachusetts’ IOLTA program was established in 1985. *Id.* at 968. Participation in the program remained voluntary from 1985 to 1990. *Id.* At the end of 1989, the Massachusetts Supreme Judicial Court converted the voluntary IOLTA program into a mandatory program, effective January 1, 1990. *Id.*

<sup>81</sup> Specifically, the plaintiffs claimed that interest being earned on their money, while held in trust, was being used to fund ideological and political causes they found to be offensive. *Id.* at 970. The client alleged that she was being forced to “choose between employing an attorney or financially supporting organizations with which she disagrees.” *Id.* However, one cannot escape the thought that the client had a third alternative; that of depositing a large enough sum of money with the attorney to justify opening a separate interest bearing account solely for the benefit of that client. This, of course, presupposes the fact that any unused portion of the retainer would be refundable.

<sup>82</sup> At the time of this case, sixty-seven percent of all interest collected from IOLTAs in Massachusetts was being channeled to Massachusetts Legal Assistance. *Id.* at 969. The remaining money was being delegated to “other designated charitable entities.” *Id.*

<sup>83</sup> *Washington Legal Foundation* also claimed that Massachusetts’ mandatory IOLTA program violated the Fifth Amendment to the United States Constitution by effecting a taking of the client’s property without just compensation. *Id.* at 970. For more information on this portion of the opinion, see *infra* Part III.B.- IV.

<sup>84</sup> *Washington Legal*, 993 F.2d at 970.

<sup>85</sup> *Washington Legal Found. v. Mass. Bar Found.*, 795 F.Supp. 50 (D. Mass. 1992).

The United States First Circuit Court of Appeals stated that analyzing appellant's First Amendment argument requires a two step process.<sup>86</sup> First, the court must determine whether Massachusetts' mandatory IOLTA program "burdens protected speech by forcing expression through compelled support of organizations espousing ideologies or engaging in political activities."<sup>87</sup> Second, if the court finds the speech to be burdened, the court will then strictly scrutinize<sup>88</sup> the Massachusetts IOLTA program to determine whether it served a compelling state interest in a narrowly tailored fashion.<sup>89</sup>

In applying the first part of the test, the court held that Massachusetts mandatory IOLTA program did not compel<sup>90</sup> appellant's speech.<sup>91</sup> While the court recognized that the interest earned on IOLTAs in Massachusetts was being used to fund activities which may be contrary to appellant's beliefs, the court reasoned that the earned interest was not the client's property, and therefore, it was not the client who was supporting the activities.<sup>92</sup>

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<sup>86</sup> *Washington Legal*, 993 F.2d at 977.

<sup>87</sup> *Id.*

<sup>88</sup> The test of 'strict scrutiny,' used in many "content-based" freedom of speech cases, is an exacting standard that requires a state to prove that its burden on speech is narrowly tailored to achieve a compelling state interest. *See, e.g.,* *Simon & Schuster, Inc. v. Members of New York State Crime Victims Bd.*, 502 U.S. 105 (1991); Carol M. Grieb, "*Son of Sam*" *Laws - A Content Based Financially Burdensome Speech Restriction That Is Not Narrowly Tailored to Achieve a Compelling State Interest is Inconsistent with the First Amendment*, 31 DUQ. L. REV. 401 (1993). Burdens on speech subject to the Court's strict scrutiny analysis rarely survive. For a case where a state law survived strict scrutiny analysis, see *Burson v. Freeman*, 504 U.S. 1919 (1971) (stating that "[i]t is the rare case in which we have held that a law survives strict scrutiny. This, however, is such a case."). *Burson* involved a challenge to a Tennessee law creating an "election-day 'campaign-free zone'" which was "designed to protect potential voters from intimidation and to conduct elections with integrity and reliability." *Id.*; see Kenneth P. Kayal, Note, *State Statute Prohibiting the Solicitation of Votes and the Display or Distribution of Campaign Materials Within 100 Feet of Polling Place Constitutes a Valid Content-Based Restriction on Protected Speech - Burson v. Freeman*, 3 SETON HALL CONST. L.J. 525 (1993).

<sup>89</sup> *Washington Legal*, 993 F.2d at 977.

<sup>90</sup> For more on the "Compelled Speech Doctrine," see Kari Thoe, Note, *A Learning Experience: Discovering the Balance Between Fees-Funded Public Fora and Compelled-Speech Rights at American Universities*, 82 MINN. L. REV. 1425 (1998); David W. Ogden, *Is There a First Amendment "Right to Remain Silent"? - The Supreme Court's "Compelled Speech" Doctrine*, 40 FED. B. NEWS & J. 368 (1993).

<sup>91</sup> *Washington Legal*, 993 F.2d at 980. Having found that the mandatory Massachusetts IOLTA program does not burden speech, the court did not see the need to reach the second step of the analysis. *Id.*

<sup>92</sup> *Id.* The court in essence merged *Washington Legal Foundation's* First and Fifth Amendment challenges to Massachusetts' IOLTA program. The appellants did not have a property interest in the "beneficial use" of the earned interest, negating the Fifth Amendment argument, so they could not plausibly state that they were being compelled to support ideological or political activities contrary to their beliefs; which negates the First Amendment argument. For more on Fifth Amendment challenges to IOLTAs, see *infra* Part III.B.

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Similarly, in *Washington Legal Foundation v. Texas Access to Justice Foundation*,<sup>93</sup> appellants claimed that their compelled participation in the Texas IOLTA program<sup>94</sup> forced them to support speech they found to be offensive,<sup>95</sup> and it violated their First Amendment right to freedom of speech.<sup>96</sup>

The district court granted the Texas Equal Access to Justice Foundation's motion for summary judgment ruling that clients do not have a property interest in funds generated by their trust accounts and that mandatory participation in the IOLTA program did not constitute financial support by the plaintiffs of the recipient organization.<sup>97</sup> The United States Fifth Circuit Court of Appeals rejected the district court's ruling, finding that clients do have a property interest in funds generated by their trust accounts.<sup>98</sup> However, the appellate court did not address the issue whether compelled participation in the Texas mandatory IOLTA program constitutes financial support by the plaintiffs of the recipient organizations.

While the Fifth Circuit did not rule specifically on the plaintiff's First Amendment claim, it did open the door by rejecting the prevailing view<sup>99</sup> that interest earned on IOLTAs was not the property of the client.<sup>100</sup>

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<sup>93</sup> 94 F.3d 996 (5<sup>th</sup> Cir. 1996) (*Texas Equal Access*), *aff'd in part by Phillips v. Washington Legal Found.*, 118 S. Ct. 1925 (1998).

<sup>94</sup> The Texas IOLTA program was established in 1984. *Id.* at 998. Participation in the Texas program was voluntary until 1988, when the Texas Supreme Court mandated participation. *Id.* at 999. Prior to the switch, the Texas IOLTA program generated approximately one million dollars per year, which was in turn distributed to various non-profit organizations. *Id.* After the switch to mandatory participation, Texas saw a dramatic increase in IOLTA revenue. *Id.* As of 1995, Texas IOLTA programs were generating nearly ten million dollars a year. *Id.*

<sup>95</sup> Specifically, the plaintiffs objected to the portion of IOLTA funds that went to groups "providing aid services to refugees seeking political asylum in the United States and those organizations assisting death row inmates to challenge their death sentences." *Texas Equal Access*, 94 F.3d at 999.

<sup>96</sup> *Id.* Washington Legal Foundation also claimed that the Texas' mandatory IOLTA program violated the Fifth Amendment to the United States Constitution. *Id.* For more information on this portion of the opinion, see *infra* Part III.B; *infra* Part IV.

<sup>97</sup> *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 873 F. Supp. 1 (W.D. Tex. 1995), *rev'd in part by Texas Equal Access*, 94 F.3d 996.

<sup>98</sup> *Texas Equal Access*, 94 F.3d at 996. This portion of the district court's holding was not only vacated by the Fifth Circuit's opinion, it has also been rejected by the United States Supreme Court. See *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925 (1998). For more on the *Phillip's* decision, see *infra* Part IV.B and Elrich, *supra* note 5, at 897 (providing an overview of the *Washington Legal Foundation v. Texas Access to Justice Foundation* decision).

<sup>99</sup> See, e.g. *Washington Legal Found. v. Massachusetts Bar Found.*, 993 F.2d 962 (1<sup>st</sup> Cir. 1993); *Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987). For a look at an early decision holding that a client has a property interest in IOLTA generated interest, see *In re Indiana State Bar Ass'ns Petition*, 550 N.E.2d 311 (Ind. 1990) (*per curiam*).

<sup>100</sup> *Texas Equal Access*, 94 F.3d at 1005. For more on this point, see *infra* Parts III.B and IV.A-B.

### B. IOLTA and the Fifth Amendment

Traditionally, Fifth Amendment<sup>101</sup> challenges to mandatory IOLTA programs have been the most common,<sup>102</sup> and recently the most damaging.<sup>103</sup> The main premise of the challengers' argument is that the interest generated by a client's money held in trust is the property of that client, and any confiscation of that interest by the state without just compensation amounts to an impermissible "taking" prohibited by the Fifth Amendment.<sup>104</sup> Until recently, this argument has been largely unsuccessful.

In *Cone v. State Bar of Florida*,<sup>105</sup> Cone<sup>106</sup> claimed that Florida's IOLTA program<sup>107</sup> constituted a 'taking' of her property without just compensation as prohibited by the Fifth Amendment to the United States Constitution.<sup>108</sup> In making her argument, Cone heavily relied on *Webb's Fabulous Pharmacies, Inc. v. Beckwith*,<sup>109</sup>

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<sup>101</sup> The Fifth Amendment to the United States Constitution reads in pertinent part: "No person . . . shall be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation." U.S. CONST. amend. V. (emphasis added). The Fifth Amendment is made applicable to the states through the Fourteenth Amendment. See, e.g., *Palko v. Connecticut*, 302 U.S. 319 (1937).

<sup>102</sup> See, e.g., *Texas Equal Access*, 94 F.3d 996; *Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962 (1<sup>st</sup> Cir. 1993); *Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987).

<sup>103</sup> See *Texas Equal Access*, 94 F.3d at 999.

<sup>104</sup> A "taking" is impermissible if "just compensation" is not provided. See U.S. CONST. amend. V. In the past, courts have been slow to recognize even a property interest on the part of the client in the IOLTA generated interest. See, e.g., *Washington Legal*, 993 F.2d at 962 (holding that a client does not possess a property interest in IOLTA generated interest); *Cone*, 819 F.2d at 1002 (holding that a client does not possess a property interest in IOLTA generated interest); see also *id.* at 1006 n.5 (listing various state supreme courts that have also failed to find a property interest on the part of the client in IOLTA generated interest). Therefore, most courts have not reached the "impermissible taking" issue. Cf. *Washington Legal*, 993 F.2d at 962 (stating *arguendo* the court's analysis of the "taking" issue).

<sup>105</sup> 819 F.2d 1002 (11<sup>th</sup> Cir. 1987).

<sup>106</sup> The suit was initially brought by Ms. Glaeser, who died while the appeal from the lower court's dismissal was pending. *Id.* at 1004. Ms. Jean Cone was the personal representative of Ms. Glaeser's estate. *Id.*

<sup>107</sup> Florida was the first state to implement an IOLTA program. *In re Interest on Trust Accounts*, 402 So. 2d 389, 396 (Fla. 1981).

<sup>108</sup> *Cone*, 819 F.2d at 1004. Specifically, Cone claimed that the interest earned on her money while held in trust in the IOLTA was her property. *Id.* Consequently, Cone claimed that the seizure of that property by the State Bar without just compensation constituted an impermissible taking. *Id.* Remarkably, the controversy in *Cone* arose over the two dollar and twenty-five cents worth of interest generated by a principal of thirteen dollars and seventy-five cents held in an IOLTA. *Id.* at 1002.

<sup>109</sup> 449 U.S. 155 (1980). In *Webb's*, the United States Supreme Court struck down a Florida law declaring interest earned on interpleader funds to be the property of the court clerk. *Id.* at 164-65. The Court relied on the general property rule that 'interest follows principal' to hold that the retention of the interest earned on the interpleader funds constituted an impermissible taking. *Id.*

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and the traditional property doctrine that “interest follows principal.”<sup>110</sup> However, the United States Eleventh Circuit Court of Appeals noted that without Florida’s IOLTA program, no interest would have been generated for the benefit of Cone or anyone else.<sup>111</sup> Therefore, the operation of Florida’s IOLTA could not be said to deprive Cone of a property interest.<sup>112</sup> The court further distinguished *Webb*’s from the case at bar by stating that the crucial distinction is in the circumstances that create “a legitimate expectation of interest exclusive of administrative costs and expenses.”<sup>113</sup> The court stated that the \$90,000 in interest involved in *Webb*’s created the necessary expectation, whereas the \$2.25 of earned interest involved in *Cone* did not.<sup>114</sup>

Similarly, in *Washington Legal Foundation v. Massachusetts Bar Foundation*,<sup>115</sup> the Foundation claimed that the Massachusetts IOLTA program<sup>116</sup> constituted a ‘taking’ of a client’s property without just compensation as prohibited by the Fifth Amendment.<sup>117</sup> Realizing that many courts have been slow to recognize a property interest in IOLTA generated interest,<sup>118</sup> the Foundation did not claim a property interest in the interest itself, but rather in the “beneficial use of the deposited funds, and more specifically, the right to control and to exclude others from the beneficial use of those funds.”<sup>119</sup> The United States First Circuit Court of Appeals began its analysis by stating that it is the plaintiff’s burden to first establish that they have a recognized property interest that is

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<sup>110</sup> *Cone*, 819 F.2d at 1004 (citing *Himely v. Rose*, 9 U.S. (5 Cranch) 313, 319 (1809)); see also *Webb’s Fabulous Pharmacies*, 449 U.S. at 155.

<sup>111</sup> *Cone*, 819 F.2d at 1004.

<sup>112</sup> *Id.*

<sup>113</sup> *Cone*, 819 F.2d at 1007.

<sup>114</sup> *Cone*, 819 F.2d at 1007. The court stated “We do not wish to imply that the state may constitutionally appropriate property so long as the property is very small property.” *Id.* Regardless, the court in *Cone* felt that the \$90,000 dollar in interest at issue in *Webb* was sufficient to warrant protection, while the \$2.25 in *Cone* was not. The court stated “The district court concluded as a matter of law that the use of . . . [Cone’s] money had no net value, therefore there could be no property interest for the state to appropriate. We agree.” *Id.* The district court had reasoned that the \$2.25 generated in interest would not have been enough to offset the administrative charges associated with placing Cone’s funds in an individual interest bearing account. *Id.* But see Kenneth Paul Kreider, Note, *Florida’s IOLTA Program does Not “Take” Client Property For Public Use: Cone v. State Bar of Florida*, 57 U. CIN. L. REV. 369, 370 (1988) (suggesting that the line of reasoning used by the court in *Cone* would be “subject to re-examining by later courts”).

<sup>115</sup> 993 F.2d 962 (1<sup>st</sup> Cir. 1993).

<sup>116</sup> For more on the Massachusetts IOLTA program, see *supra* notes 80-82 and accompanying text. The Washington Legal Foundation also claimed that the Massachusetts IOLTA program violated their First Amendment right to freedom of speech. See *supra* Part III.A.

<sup>117</sup> See U.S. CONST. amend. V. For the pertinent text of the Fifth Amendment, see *supra* note 101.

<sup>118</sup> See *Washington Legal*, 993 F.2d at 973 (citing five cases where courts have refused to recognize a client’s property interest in interest earned on an IOLTA).

<sup>119</sup> *Id.*



capable of being protected under the Fifth Amendment.<sup>120</sup> Here, the Foundation asserted that a client's right to control the beneficial use of the IOLTA generated interest is a protected property interest based in trust law.<sup>121</sup> The Foundation asserted that because the phrase "Interest on Lawyers' Trust Accounts" contained the word "trust", a trust<sup>122</sup> is created between the client and the attorney when the client's money is deposited into an IOLTA.<sup>123</sup> The circuit court rejected the Foundation's trust argument, stating that the relationship between attorney and client in Massachusetts is a fiduciary relationship as a matter of law.<sup>124</sup> Specifically, the circuit court stated "we are not convinced that the deposit of client's funds into IOLTA accounts transforms a lawyer's fiduciary obligation to clients into a formal trust with the reserved right by the client to control the beneficial use of the funds."<sup>125</sup> The circuit court similarly rejected the Foundation's claim that a client has a protected property right to exclude others from the beneficial use of their property.<sup>126</sup> In doing so, the court distinguished the recognized right to exclude others from one's real property,<sup>127</sup> from trying to exclude others from one's intangible property.<sup>128</sup> The court found no support for the proposition that a person has a constitutionally protected right to exclude others from intangible property.<sup>129</sup> The First Circuit Court's decision in *Washington Legal* proved to be the high water mark in courts finding IOLTAs constitutionally valid.<sup>130</sup>

#### IV. IOLTA, PRESENT AND FUTURE

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<sup>120</sup> *Id.* The court noted that not all property interests are protected by the U.S. Constitution. *Id.*; see also *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155, 161 (1980) (stating that "a mere unilateral expectation or an abstract need is not a property interest entitled to protection").

<sup>121</sup> *Washington Legal*, 993 F.2d at 974.

<sup>122</sup> A "trust" is defined as a legal entity created by a grantor for the benefit of designated beneficiaries under the laws of the state and the valid trust agreement. BLACK'S LAW DICTIONARY 1221 (6<sup>th</sup> ed. 1990). The trustee has a fiduciary duty to manage the trust's corpus assets and income for the economic benefit of all the beneficiaries. *Id.*

<sup>123</sup> See *Washington Legal*, 993 F.2d at 974.

<sup>124</sup> *Id.*

<sup>125</sup> *Id.*

<sup>126</sup> *Id.* The Foundation was relying exclusively on cases where the United States Supreme Court had recognized a property interest in excluding others from the beneficial use of real property. *Id.*; see, e.g. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982); *infra* note 127.

<sup>127</sup> *Washington Legal*, 993 F.2d at 974; see also *Kaiser Aetna v. United States*, 444 U.S. 164 (1979) (holding that the government's attempt to create a free right to public access to a pond constituted a taking); *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982) (holding that a governmentally authorized installation of cable television equipment constituted a taking); Robert D. Rubin, *Taking Clause v. Technology: Loretto v. Teleprompter Manhattan CATV, A Victory For Tradition*, 38 U. MIAMI L. REV. 165 (1983); Catherine R. Connors, Comment, *Appalachian Electric Revisited: The Recapture Provision of the Federal Power Act After Nollan and Kaiser Aetna*, 40 DRAKE L. REV. 533 (1991).

<sup>128</sup> *Washington Legal*, 993 F.2d at 974.

<sup>129</sup> *Id.*

<sup>130</sup> See *infra* Part IV.A-B.

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## THE FUTURE OF IOLTA

At about the same time the First Circuit<sup>131</sup> was joining the Eleventh Circuit<sup>132</sup> in declaring that a client has no property interest in IOLTA generated interest, a controversy over the same issue was brewing in Texas.<sup>133</sup> The follow two decisions mark the turning of the tide against IOLTAs.

A. *Washington Legal Foundation v. Texas Access to Justice Foundation*

In *Washington Legal Foundation v. Texas Access to Justice Foundation*,<sup>134</sup> the Texas IOLTA program was challenged on grounds that it constitutes an impermissible ‘taking’ of a client’s property without just compensation in dereliction of the Fifth Amendment to the United States Constitution.<sup>135</sup>

The United States Fifth Circuit Court of Appeals reversed the district court’s ruling<sup>136</sup> that a client did not have a property interest in IOLTA generated interest.<sup>137</sup> The court of appeals began its analysis by noting that Texas follows the traditional rule that “interest follows principal”.<sup>138</sup> The court stated that “in light of this rule, it seems obvious that the interest earned in the IOLTA accounts is the property of the clients whose money is held in those accounts.”<sup>139</sup> The court also relied on the reasoning of the United States Supreme Court in *Webb’s Fabulous Pharmacies, Inc. v. Beckwith*<sup>140</sup> that “earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property.”<sup>141</sup> In refusing to follow the lines of reasoning used by the First<sup>142</sup> and Eleventh Circuits,<sup>143</sup> the Fifth Circuit created a split of authority on the constitutionality of mandatory IOLTAs. Consequently, the respondents in the

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<sup>131</sup> *Supra* Part III.B (discussing *Washington Legal*, 993 F.2d 962).

<sup>132</sup> *Supra* Part III.B (discussing *Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987)).

<sup>133</sup> *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 873 F. Supp. 1 (W.D. Tex. 1995), *rev’d in part by* *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 94 F.3d 996 (5<sup>th</sup> Cir. 1996).

<sup>134</sup> 94 F.3d 996 (5<sup>th</sup> Cir. 1996).

<sup>135</sup> *Id.* at 999.

<sup>136</sup> *See Texas Equal Access*, 873 F.Supp. at 8. Specifically, the lower court held that a client had neither a property interest in the IOLTA generated interest, nor a protected property interest in the “beneficial use” of the IOLTA generated interest. *Id.* In making these determinations, the lower court heavily relied on the decisions in *Cone* and *Washington Legal Foundation v. Massachusetts Bar Foundation*.

<sup>137</sup> *Texas Equal Access*, 94 F.3d at 996.

<sup>138</sup> The traditional “interest follows principal” rule that the court alluded to stands for the proposition that “interest earned on a deposit of principal belongs to the owner of that principal.” *Id.* at 1000 (citing *Sellers v. Harris County*, 483 S.W.2d 242, 243 (Tex. 1972)).

<sup>139</sup> *Id.*

<sup>140</sup> 449 U.S. 155 (1980).

<sup>141</sup> *Id.* at 162-63; *see generally* *Torregrossa*, *supra* note 40; *Douglas*, *supra* note 14.

<sup>142</sup> *See Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962 (1<sup>st</sup> Cir. 1993); *see supra* Part III.B.

<sup>143</sup> *See Cone v. State Bar of Florida*, 819 F.2d 1002 (11<sup>th</sup> Cir. 1987); *see supra* Part III. B.

*Texas Access* were granted a writ of certiorari<sup>144</sup> by the United States Supreme Court.<sup>145</sup>

### B. *Phillips v. Washington Legal Foundation*

In *Phillips v. Washington Legal Foundation*,<sup>146</sup> a sharply divided Court<sup>147</sup> affirmed the Fifth Circuit Court's ruling that "the interest income generated by funds held in IOLTA accounts is the 'private property' of the owner of the principal."<sup>148</sup> The Court relied on its prior holding in *Webb's Fabulous Pharmacies v. Beckwith*<sup>149</sup> that interest follows principal.<sup>150</sup> The Court denied petitioner's arguments that Texas did not follow

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<sup>144</sup> "Writ of certiorari" is defined as:

An order by the . . . [Supreme Court] which is used by that court . . . on whether or not to hear an appeal from a lower court . . . In the U.S. Supreme Court, a review on writ of certiorari is not a matter of right, but of judicial discretion, and will be granted only when there are special and important reasons therefor.

BLACK'S LAW DICTIONARY 1609 (6<sup>th</sup> ed. 1990).

<sup>145</sup> *Phillips v. Washington Legal Found.*, 117 S. Ct. 2535 (1997). The Court limited the writ of certiorari to the following question:

Is interest earned on client trust funds held by lawyers in IOLTA accounts a property interest of the client or lawyer, cognizable under the Fifth Amendment of the United States Constitution, despite the fundamental precept of IOLTA that such funds, absent the IOLTA program, could earn interest for the client or lawyer?

Petitioner's Brief at 1, *Phillips* (No. 96-1578). At this juncture, the Court declined to consider whether the state's use of the IOLTA generated interest constituted a "taking", if in fact, the Court held the interest to be the property of either the client or the lawyer. This issue was to be decided on remand. See *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1934 (1998) (stating "we express no view to whether these funds have been 'taken' by the State . . . [W]e leave these issues to be addressed on remand").

<sup>146</sup> 118 S. Ct. 1925 (1998).

<sup>147</sup> The vote was 5-4. *Id.* at 1925. Chief Justice Rehnquist authored the opinion while Justices Souter, Stevens, Ginsburg and Breyer dissented. *Id.* at 1927. The dissent felt that the Court's analysis and holding only partially addressed the "takings" issue. *Id.* at 1934 (Souter, J., dissenting). Justice Souter stated that "The Court recognizes three distinct issues implicated by a takings claim: whether the interest asserted by the plaintiff is property, whether the government has taken that property, and whether the plaintiff has been denied just compensation for the taking. The Court is careful to address only the first of these questions." *Id.* (citations omitted). Justice Souter's approach would be for the Court to "determine here whether either of the remaining issues might reasonably be resolved against [Phillips]; if so, we should not abstract the property issue for resolution in their now." *Id.* at 1935-36.

A separate dissent was authored by Justice Breyer. *Id.* at 1937 (Breyer, J., dissenting). Justice Breyer agreed with Justice Souter that the Court should analyze the three issues presented by a "takings" claim collectively. *Id.* However, Justice Breyer also thought the majority's conclusion on the question presented was incorrect. *Id.* at 1938. Justice Breyer distinguished the majority's reliance on *Webb's Fabulous Pharmacies* and would have held that a client does not have a property interest in IOLTA generated interest. *Id.* at 1939.

<sup>148</sup> *Id.* at 1934.

<sup>149</sup> 449 U.S. 155 (1980)

<sup>150</sup> *Phillips*, 118 S. Ct. at 1931 (stating "at least as to confiscatory regulations, . . . a State

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 the “interest follows principal” rule<sup>151</sup> and that client money held in an IOLTA could not reasonably be expected to generate interest income.<sup>152</sup> The Court further stated that the analysis of whether an object is property does not rest on whether it possesses economic value.<sup>153</sup> The Court reasoned that “while the interest income at issue here may have no economically realizable value to its owner, possession, control, and disposition are nonetheless valuable rights that inhere in the property”.<sup>154</sup> Having concluded that a client has a cognizable property interest in IOLTA generated interest, the Court remanded the case back to the Fifth Circuit Court to decide the remaining issues.<sup>155</sup>

### C. Do IOLTAs “Take”?

The United States Supreme Court recognizes that a takings claim consists of three distinct issues: (1) whether there is a property interest at stake; (2) whether the government has taken that property; and (3) whether just compensation is required.<sup>156</sup> Having decided the first of these issues in favor of the Washington Legal Foundation,<sup>157</sup> the Court charged the Fifth Circuit Court of Appeals with the task of determining whether IOLTA’s “take” property of the client.<sup>158</sup>

In the past, the United States Supreme Court has stated that analyzing ‘takings’ claims does not involve the use of a bright line rule but rather, courts must “engag[e] in

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may not sidestep the Takings Clause by disavowing traditional property interest long recognized under state law.”).

<sup>151</sup> Petitioner based their argument that Texas does not blindly follow the “interest follows principal” rule on several exceptions recognized by Texas law. *Id.* at 1931. One exception involved “income-only trusts” and another “marital community property.” *Id.* In Texas, neither of these exceptions utilize the traditional “interest follows principal” rule. *Id.* The Court distinguished these types of exceptions by noting that both exceptions had a “firm basis in traditional property law principles.” *Id.* Whereas there are no similar traditional principles of property law that support the proposition that “the owner of a fund temporarily deposited in an attorney trust account may be deprived of the interest the fund generates.” *Id.*

<sup>152</sup> *Id.* at 1932 (citing *Cone v. State Bar of Florida*, 819 F.2d 1002, 1007 (11<sup>th</sup> Cir. 1987)).

<sup>153</sup> *Id.* at 1933. The Court states “Property is more than economic value, it also consists of the group of rights which the so-called owner exercises in his dominion over the physical thing, such as the right to possess, use and dispose of it.” *Id.* (citing *United States v. General Motors Corp.*, 65 U.S. 357, 359 (1945)); *see also* *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982).

<sup>154</sup> *Phillips*, 118 S. Ct. at 1933; *see Hodel v. Irving*, 481 U.S. 704, 715 (1987) (holding that the right to “pass on” property was a valuable right).

<sup>155</sup> *Phillips*, 118 S. Ct. at 1934. The remaining two issues to be decided on remand are discussed in detail *infra* Part IV.C-D.

<sup>156</sup> *Phillips*, 118 S. Ct. at 1934.

<sup>157</sup> *Id.*

<sup>158</sup> *Id.* The Fifth Amendment to the United States Constitution prohibits a “taking” without “just compensation.” U.S. CONST. amend. V. For an in-depth historical analysis of the taking issue, *see* F. BOSSELMAN ET AL., *THE TAKING ISSUE* (1973). The just compensation requirement is discussed *infra* Part IV.D.

. . . essentially ad hoc, factual inquiries.”<sup>159</sup> In conducting these inquiries, the Court has articulated several useful factors to aid the courts.<sup>160</sup> For the purpose of analyzing Fifth Amendment “takings” claims, the Court has stated that the “economic impact of the regulation on the claimant,”<sup>161</sup> the “extent to which the regulation has interfered with distinct investment backed expectations,”<sup>162</sup> and “the character of the governmental action,”<sup>163</sup> are all relevant in determining whether there has been a taking.<sup>164</sup>

Application of the “economic impact of the regulation on the claimant”<sup>165</sup> factor, as it applies to *Phillips*,<sup>166</sup> seems relatively straight forward.<sup>167</sup> Since the Court has already determined in *Phillips* that the client has a property interest in IOLTA generated interest,<sup>168</sup> any “taking” of that property would surely seem to have an economic

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<sup>159</sup> Penn Cent. Trans. Co. v. New York City, 438 U.S. 104, 124 (1978); see also David Schultz, *Scalia, Property, and Dolan v. Tigar: The Emergence of a Post Caroline Products Jurisprudence*, 29 AKRON L. REV. 1 (1995) (stating that Justice Scalia has voted in favor of the property owner eighty-nine percent of the time).

<sup>160</sup> See *Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962, 974 (1<sup>st</sup> Cir. 1993) (citing Penn Cent. Trans. Co. v. New York City, 438 U.S. 104, 124 (1978)); see also *Eastern Enterprises v. Apfel*, 118 S. Ct. 2131 (1998); *Connolly v. Pension Benefit Guar. Corp.*, 475 U.S. 211 (1986); *Kaiser Aetna v. United States*, 444 U.S. 164 (1979).

<sup>161</sup> *Connolly*, 475 U.S. at 225.

<sup>162</sup> *Id.*

<sup>163</sup> *Id.* For more on these three factors and how they have changed since the Court’s decision in *Penn Central*, see David L. Callies, *Property Right since Penn Central: Regulatory Takings, Investment-Backed Expectations, and Economically Beneficial Use: How Perspectives on Property Rights Have Changed From Penn Central to Lucas*, SB14 A.L.I.-A.B.A. 171 (Continuing Legal Education, Oct. 17, 1996), available in Westlaw, SB14 ALI-ABA 171.

<sup>164</sup> See *Penn Central*, 438 U.S. at 124. *Penn Central* involved a challenge to a city ordinance which in effect prohibited the development of private property deemed to be a scenic or historic landmark. *Id.* While the Court upheld the regulation, it laid out the factors that have governed courts “taking” inquiries for the past twenty years. *Id.*; see generally Daniel T. Cavarelo, Comment, *From Penn Central to United Artists’ I & II: The Rise to Immunity of Historic Preservation Designation from Successful Takings Challenges*, 22 BC ENVTL. AFF. L. REV. 593 (1995).

<sup>165</sup> *Connolly v. Pension Benefit Guaranty Corp.*, 475 U.S. 211, 225 (1986).

<sup>166</sup> *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925 (1998).

<sup>167</sup> The dissent in the *Phillips* case would not so readily agree. See *id.* at 1936 (Souter, J., dissenting) (maintaining that there has been “no physical occupation or seizure of tangible property”). But see *Eastern Enterprises v. Apfel*, 118 S. Ct. 2131, 2146 (1998) (quoting Penn Cent. Trans. Co. v. New York City, 438 U.S. 104, 124 (1978)) (stating “although takings problems are more commonly presented when ‘the interference with property can be characterized as a physical invasion by government, than when interference arises from some public program adjusting the benefits and burdens of economic life to promote the common good,’ economic regulations . . . nonetheless effect a taking.”).

<sup>168</sup> *Phillips*, 118 S. Ct. at 1934; cf. *Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962, 974 (1<sup>st</sup> Cir. 1993) (stating in dicta that IOLTAs “cause an illegal ‘taking’”). However, the First Circuit in *Washington Legal Foundation v. Massachusetts Bar*

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 impact on the client.<sup>169</sup> The only apparent hurdle to this line of reasoning is the argument that under current law, interest earned on NOW type accounts cannot be paid into a pooled client trust account, albeit for the benefit of a charitable organization.<sup>170</sup> The argument proceeds that the client as an individual can not receive interest on his deposit into a pooled client trust account,<sup>171</sup> and therefore the subsequent confiscation of that interest by the government does not economically impact the client.<sup>172</sup> However, the Court has already held that a client has a property interest in IOLTA generated interest.<sup>173</sup> Consequently, a line of reasoning that would deny the client the economic benefit of that interest, solely on the grounds that a client does not currently have access to it,<sup>174</sup> appears to be circular. This outcome appears even more unjust when one considers that the client's participation in the IOLTA program is mandated by the very entity seeking to confiscate the interest earned on the client's principle. Further, the fact that the confiscated interest would be used to fund worthwhile public concerns<sup>175</sup> should not be controlling. In *Armstrong v. U.S.*,<sup>176</sup> the United States Supreme Court stated that the purpose of the Takings Clause is to prevent the government "from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole."<sup>177</sup>

Similarly, it would be difficult to assert that a client cannot satisfy the second of the *Penn Central* factors, that of a "distinct investment backed expectation."<sup>178</sup> The United

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*Foundation* based its dicta finding on the proposition that a client does not have a recognizable property right in the IOLTA generated interest. *Id.* at 975. A proposition that has been rejected by the United States Supreme Court in *Phillips*. See *Phillips*, 118 S. Ct. at 1934.

<sup>169</sup> See Amanda French Palmer, Comment, *A Critique of Interest on Lawyers' Trust Account Programs*, 44 LA. L. REV. 999, 1020-21 (1984) (concluding in 1984 that IOLTA's violate the Takings Clause of the U.S. Constitution); cf. Dulong, *supra* note 36 (concluding that IOLTAs are consistent with the Takings Clause); see also Douglas, *supra* note 14 (reaching the same conclusion as Palmer, *supra*, thirteen years later).

<sup>170</sup> See 12 U.S.C. § 1832(a)(2). Interest on these types of accounts may only be paid to individuals or certain types of exempt organizations. *Id.*; *supra* notes 29-31 and accompanying text.

<sup>171</sup> 12 U.S.C. § 1832; see *supra* notes 29-31 and accompanying text.

<sup>172</sup> See, e.g., *Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962, 976 (1<sup>st</sup> Cir. 1993); *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1936 (1998) (Souter, J., dissenting).

<sup>173</sup> *Phillips*, 118 S. Ct. at 1934.

<sup>174</sup> See, e.g., *Washington Legal*, 993 F.2d at 976; *Phillips*, 118 S. Ct. at 1936 (Souter, J., dissenting).

<sup>175</sup> See *supra* notes 2, 7, 13 and accompanying text.

<sup>176</sup> 364 U.S. 40 (1960). For an indepth look at the Court's decision in *Armstrong* and it's application to compensation statutes, see William Michael Treanor, *The Armstrong Principle, The Narratives of Takings, and Compensation Statutes*, 38 WM. & MARY L. REV. 1151 (1997).

<sup>177</sup> *Armstrong*, 364 U.S. at 40.

<sup>178</sup> *Penn Cent. Trans. Co. v. New York City*, 438 U.S. 104, 124 (1978); see also *Connolly v. Pension Benefit Guaranty Corp.*, 475 U.S. 211, 225 (1986); Chauncey L. Walker and Scott D. Avitable, *Regulatory Takings, Historic Preservation and Property Rights Since Penn Central: The Move Toward Greater Protection*, 6 FORDHAM ENVTL. L.J. 819 (1995)

States Supreme Court has itself created such an expectation by declaring that a client has a property interest in IOLTA generated interest.<sup>179</sup> Surely, any client who knows that money held in trust is capable of earning interest would expect that the interest be paid to him rather than a fund to support political or ideological groups with which he may not agree.<sup>180</sup> The mere fact that a client may not necessarily consider his deposit into an IOLTA an ‘investment’ in the traditional sense of the word,<sup>181</sup> cannot be said to preclude that same client from expecting to receive the interest once the United States Supreme Court has declared it his property.<sup>182</sup>

The third *Penn Central* factor calls for a factual inquiry into “the character of the governmental action.”<sup>183</sup> While in the past the Court has stated that takings problems are more commonly presented when “the interference with property can be characterized as a physical invasion by government,”<sup>184</sup> the Court has also stated that “public program[s] adjusting the benefits and burdens of economic life to promote the common good can . . . nonetheless effect a taking.”<sup>185</sup>

In the case of IOLTAs, the states have attempted to fund legal-aid organizations<sup>186</sup> by siphoning off the interest generated by a client’s money being held in trust. On remand, the Fifth Circuit Court will need to balance competing interests.<sup>187</sup> Namely, the use of a client’s property to promote the public good versus the apparent injustice of requiring “a dispersed political minority”<sup>188</sup> to bear, what in all fairness is the public’s burden of funding legal service for the disadvantaged.<sup>189</sup>

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(explaining/discussing the evolution of the Penn Central doctrine).

<sup>179</sup> *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1934 (1998).

<sup>180</sup> *Washington Legal Found. v. Mass. Bar Found.*, 993 F.2d 962 (1<sup>st</sup> Cir. 1993); *see supra* Part III.A.

<sup>181</sup> This is not to say that a client would not view depositing money into an attorney’s trust as an investment. One could always assert that clients retain attorneys with the expectation, or at the very least, hope, that they will recover from the defendant more than the cost of their representation. Otherwise, basic principles of economics would dictate that the client not pursue his claim. This being the case, any additional returns, such as interest earned on a client’s funds while held in trust, are merely an incidental return on the client’s “distinct investment backed expectations.” *See Connolly v. Pension Benefit Guar. Corp.*, 475 U.S. 211, 225 (1986).

<sup>182</sup> *See Phillips*, 118 S. Ct. at 1934.

<sup>183</sup> *Penn Central*, 438 U.S. at 124.

<sup>184</sup> *Id.*

<sup>185</sup> *Id.*

<sup>186</sup> *See supra* notes 2-7 and accompanying text.

<sup>187</sup> *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1934 (1998).

<sup>188</sup> *See Douglas, supra* note 14, at 1332 (accusing IOLTA programs of “quietly confiscating property from a dispersed political minority”). *But see* Daniel A. Farber, *Economic Analysis and Just Compensation*, 12 INT’L REV. L. & ECON. 125, 125 (1992) (suggesting that “legislatures normally offer compensation to landowners whose property is taken for a project, because they would form a powerful lobby against the project if not ‘bought off.’”).

<sup>189</sup> *See supra* notes 176-77 and accompanying text.

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Perhaps the courts<sup>190</sup> and legislature's have good intentions in devising a scheme whereby interest generated by money held in an attorney's trust account could be used to fund legal services for the disadvantaged. However, the Supreme Court has stated on prior occasion that "a strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change."<sup>191</sup>

*D. Is "Just Compensation" Due?*

If the Fifth Circuit Court of Appeals concludes that a taking has occurred, the court must then decide the third issue of whether "just compensation" is due.<sup>192</sup> In considering the issue of just compensation, the Court has traditionally sought to place the claimant "in as good a position pecuniarily as if his property had not been taken."<sup>193</sup>

Further, the claimant's loss is to be calculated objectively,<sup>194</sup> independent of the claimant's subjective valuation.<sup>195</sup>

Applying this traditional measure of compensation to *Phillip's*, the Fifth Circuit Court on remand will need to consider what the client's position would have been in the absence of his compelled participation in an IOLTA program.<sup>196</sup> Those arguing for the

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<sup>190</sup> Some IOLTA's are created by judicial decree. See Doherty, *supra* note 38, at 490.

<sup>191</sup> *Eastern Enterprises v. Apfel*, 118 S. Ct. 2131, 2146 (1998) (quoting *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 416 (1922)).

<sup>192</sup> *Phillips*, 118 S. Ct. at 1934. The Fifth Amendment to the United States Constitution prohibits a "taking" without "just compensation." U.S. CONST. amend. V.; *supra* note 101, 158. The doctrine of just compensation has been extensively explored by legal commentators in recent years. See, e.g., Lior J. Strahilevitz, Note, *When the Taking Itself Is Just Compensation*, 107 YALE L.J. 1975 (1998); Shubba Ghosh, *Takings, The Exit Option and Just Compensation*, 17 INT'L REV. L. & ECON. 157 (1997); Clynn D. Lunney, Jr., *Compensation For Takings: How Much Is Just?*, 42 CATH. U. L. REV. 721 (1993).

<sup>193</sup> *Phillips*, 118 S. Ct. at 1936 (Souter, J., dissenting) (quoting *United States v. 564.54 Acres land*, 441 U.S. 506, 510 (1979)); see also *Monongahela Navigation Co. v. United States*, 148 U.S. 312, 326 (1893) (stating claimant is entitled to a "full and exact equivalent" of that of which was taken).

<sup>194</sup> This approach has drawn sharp criticism from legal scholars. See Lunney, Jr., *supra* note 192, at 722-23 (stating "the Court has tried to pretend that its decisions regarding the proper measure of compensation are consistent with one another . . . a suggestion that . . . is no more plausible . . . than when made with respect to the Court's rulings on whether a taking has occurred."); see also D. Benjamin Barros, Note, *Defining "Property" In the Just Compensation Clause*, 63 FORDHAM L. REV. 1853, 1853-54 (1995) (suggesting that the lack of a consistent definition of 'property' has led to confusion on the issue of what is just compensation).

<sup>195</sup> *Phillips*, 118 S. Ct. at 1936 (Souter, J., dissenting). But see Marilyn F. Drees, *Do State Legislatures Have a Role in Resolving the 'Just Compensation' Dilemma? Some Lessons From Public Choice and Positive Political Theory*, 66 FORDHAM L. REV. 787, 789 (1997) (stating that legislative efforts can be used to complement those of the courts in resolving the "just compensation dilemma").

<sup>196</sup> *Phillips*, 118 S. Ct. at 1936 (Souter, J., dissenting).



continued viability of IOLTAs<sup>197</sup> will undoubtedly assert that because the client could not earn interest prior to IOLTA,<sup>198</sup> that compensation is not required to return the client to his *status quo*.<sup>199</sup> However, this argument is not entirely supported.

First a client, as an individual, can earn interest on his NOW<sup>200</sup> account, and although it is not always economically feasible to do so,<sup>201</sup> at least the choice remains with the client.<sup>202</sup> Second, the fact that a lawyer's pooled client trust account was incapable of generating interest prior to the adoption of the IOLTA concept should not be permitted to preclude the client from obtaining what is rightfully his property.<sup>203</sup> The United States Supreme Court did not let this fact stand in the way of declaring that a client has a property interest in IOLTA generated interest,<sup>204</sup> and neither should the Fifth Circuit let it stand in the way of a client receiving just compensation for the subsequent confiscation of that property interest. Finally, to say that a client is not entitled to any form of compensation would render meaningless the client's property interest in "possession, control, and disposition" of that property.<sup>205</sup> These are interests that have been deemed "valuable rights" by the United States Supreme Court.<sup>206</sup>

Once the court makes the determination that just compensation is due, the focus of the inquiry will turn to the amount of compensation required.<sup>207</sup> In the case of IOLTAs, the fact that the property taken was money makes the quantitative valuation of the compensation due rather simple. The just compensation, or amount required to make the client whole, is the exact amount of interest taken,<sup>208</sup> minus any fees the client

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<sup>197</sup> In the *Phillip's* case, this would be the Texas Access to Justice Foundation.

<sup>198</sup> See *supra* note 31 and accompanying text.

<sup>199</sup> See, e.g., *Phillips*, 118 S. Ct. at 1936 (Souter, J., dissenting).

<sup>200</sup> For a discussion of NOW accounts, see *supra* notes 29, 30 and accompanying text.

<sup>201</sup> This is due to the fact there are generally banking fees associated with the maintenance of a NOW account, and because the interest generated by these types of accounts is relatively small.

<sup>202</sup> As opposed to the situation where a client's participation in a state's IOLTA program is mandated. See *supra* notes 40, 70 and accompanying text.

<sup>203</sup> Recall that the United States Supreme Court has held that a client has a property interest in IOLTA generated interest. *Phillips*, 118 S. Ct. at 1934.

<sup>204</sup> *Id.*

<sup>205</sup> *Id.* at 1933.

<sup>206</sup> *Id.*

<sup>207</sup> For a look at the different methods courts use to arrive at a compensation figure that is just, see Lunney, Jr., *supra* note 192; Lynda J. Oswald, *Goodwill and On-Going Concern Value: Emerging Factors in the Just Compensation Equation*, 32 B.C. L. REV. 283 (1991).

<sup>208</sup> For example, if the government effects a taking of a claimant's pocket change consisting of three quarters, two dimes, and a nickel, the amount of compensation required to place the claimant "in as good a position pecuniarily as if his property had not been taken" would be one dollar. See, e.g., *Phillips*, 118 S. Ct. at 1936 (Souter, J., dissenting) (quoting *United States v. 564.54 Acres land*, 441 U.S. 506, 510 (1979)). Notice the valuation of the property becomes more difficult when the property is not money, but perhaps the goodwill of a business. For more on this point, see Oswald, *supra* note 207, at 284 (1991) (stating that a "number of state courts and legislatures have begun to recognize that losses of goodwill,

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 would have incurred by maintaining an interest bearing NOW account.<sup>209</sup>

#### V. CONCLUSION

Consideration of the *Penn Central* factor's as they apply to IOLTAs reveal that the state's confiscation of IOLTA generated interest does effect a taking.<sup>210</sup> Similarly, there does not seem to be a way of justly compensating the client absent the state's relinquishment of all IOLTA generated interest.<sup>211</sup>

While there does not appear to be any "quick fix" to the current crisis confronting IOLTAs, legislative and administrative inconveniences<sup>212</sup> resulting from potential solutions cannot be permitted to stand in the way of the constitutional command of the Fifth Amendment, that "private property [not] be taken for public use, without just compensation".<sup>213</sup>

Even if IOLTAs somehow emerge intact from the immediate threat in Texas under the Fifth Amendment,<sup>214</sup> they will undoubtedly be challenged again on First Amendment grounds,<sup>215</sup> now that the United States Supreme Court has declared that a client has a property interest in IOLTA generated interest.<sup>216</sup>

Because it seems likely that the Fifth Circuit, on remand, will find a taking requiring just compensation within the constrictors of the Fifth Amendment, an assessment needs to be made of alternative sources of funding for legal aid organizations<sup>217</sup> that will be left financially abandoned in the wake of IOLTA's apparent demise.

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going-concern value, or profits are real losses for which property owners should be compensated.").

<sup>209</sup> Cf. *Cone v. State Bar of Florida*, 819 F.2d 1002, 1006 (11<sup>th</sup> Cir. 1987).

<sup>210</sup> See *supra* Part IV.C.

<sup>211</sup> See *supra* Part IV.D.

<sup>212</sup> The administrative inconvenience would be to the attorney who would have to set up an individual NOW account for each individual client, undoubtedly at a considerable expense. However, these costs could in turn be recouped by the attorney through an increase in legal fees. Alternatively, upon commencement of the representation, the client could be asked to sign a waiver to any nominal interest his deposit would have generated, thus allowing the attorney to place the funds in a pooled client trust account, reduce his administrative costs, and spare the client the increased fees. All of this of course, presupposes the crucial fact that a client's deposit need generate enough interest to offset any banking fees associated with maintaining the NOW account.

<sup>213</sup> U.S. CONST. amend V.

<sup>214</sup> See *supra* Part IV.

<sup>215</sup> See *supra* Part III.A.

<sup>216</sup> *Phillips v. Washington Legal Found.*, 118 S. Ct. 1925, 1934 (1998). In *Washington Legal Foundation v. Massachusetts Bar Foundation*, the First Circuit Court of Appeals denied appellants relief on the grounds that a client does not have a property interest in IOLTA generated interest. 993 F.2d 962, 980 (1<sup>st</sup> Cir. 1993). This proposition has now been rejected by the United States Supreme Court. *Phillips*, 118 S.Ct. at 1934.

<sup>217</sup> See *supra* notes 2-7, 13 and accompanying text.

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