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November 13, 2008

Via U.S. Mail and E-mail to Comments@FDIC.gov

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington DC 20429

Re: RIN # 3064-AD37
Comments on IOLTA Accounts and the Transaction Account Guarantee Program

Dear Mr. Feldman:

It is the purpose of this letter to urge the Federal Deposit Insurance Corporation (the "FDIC") to extend the benefits of its Transaction Account Guarantee Program ("TAG Program") to interest-bearing trust accounts maintained by lawyers as part of their respective jurisdictions' interest on lawyers' trust accounts ("IOLTA") programs as long as those trust accounts are with banks participating in the TAG Program. I am writing as President of the National Association of IOLTA Programs ("NAIP"). IOLTA programs exist in all 50 states, the District of Columbia and the U.S. Virgin Islands.

NAIP urges the FDIC to include IOLTA accounts in the TAG Program's unlimited insurance for funds above the existing deposit insurance cap for the following reasons:

- IOLTA accounts operate in the same manner as the transaction accounts identified for coverage under the TAG Program. They also have been recognized by regulatory authorities in other contexts as substantially the same as noninterest-bearing transaction accounts. Thus, even though IOLTA accounts bear interest, both the Federal Reserve Board and the FDIC have for other purposes (i.e. addressing the Regulation D prohibition on paying interest on demand accounts) determined that IOLTA accounts should be treated the same as noninterest-bearing accounts. As a consequence of that decision, withdrawals may be made from IOLTA accounts with no advance notice and without a limitation on the number of transactions.

- Excluding IOLTA accounts from the TAG Program will destabilize these accounts and may result in lawyers to moving their IOLTA deposits to noninterest-bearing transaction accounts to obtain full coverage or relocate their IOLTA accounts from their local bank in favor of the perceived safety of a larger institution.

- The FDIC has asked whether NOW accounts held by charitable organizations or governmental units should qualify for the TAG Program guarantee. The Federal Reserve Board has determined that IOLTA accounts meet the eligibility test for NOW accounts because interest is required to be paid to a nonprofit or government entity for charitable purposes.1 Prior to this determination, funds held today in IOLTA accounts did not earn interest and were held in accounts indistinguishable from the "noninterest-bearing transaction accounts" identified for coverage in the TAG Program.

- IOLTA serves important public purposes and is the second largest dedicated source of funding for civil legal aid programs in the country. IOLTA annually benefits countless nonprofit organizations offering free help to hundreds of thousands of low-income, financially fragile individuals and families. Excluding IOLTA accounts from the TAG Program will cause significant harm to vulnerable people with civil legal problems affecting their most basic needs: safety, shelter, food, jobs and access to healthcare.

Background of IOLTA Programs and Operation of IOLTA Accounts.

Before IOLTA began in the 1980s, lawyers deposited short term and nominal client funds in noninterest-bearing checking accounts. IOLTA programs were made possible by approval from federal regulators to establish IOLTA accounts as interest-bearing transaction accounts because the entire beneficial interest in IOLTA accounts is used for charitable purposes. IOLTA programs are authorized either by State Supreme Court Rules or legislation that requires the interest to be paid to a philanthropic or governmental agency for civil legal aid to the poor, improvements in the administration of justice, educating the public about the law, and other law-related charitable public service programs. IOLTA is a vital funding source for civil legal services to the poor. Hundreds of thousands of poor individuals and families in America have received critical legal assistance as a result of this program at no cost to taxpayers. The demand for these services is only increasing in the current economic climate, including the growth in foreclosures and consumer credit problems.

Like other accounts that are eligible for coverage by participating banks under the TAG Program, IOLTA accounts are used by lawyers as payment-processing accounts to disburse funds for routine transactions such as the transfer of real estate, fees for court filings or disbursement of insurance settlements. For example, where attorneys facilitate the conveyancing of real estate, the funds of multiple parties are presented at the closing and disbursed shortly thereafter from the closing lawyer's IOLTA account.

1 See attached sample letters (for the Michigan, Maryland and New Jersey IOLTA programs recording the Federal Reserve System Board's determination that NOW accounts may be used for charitable IOLTA programs under the Consumer Checking Account Equity Act of 1980 test that the interest is paid to a philanthropic organization operated for "religious, philanthropic, charitable, educational, or other similar purposes" or to a governmental entity.

The TAG Program as Applied to IOLTA Accounts.

As you know, the TAG Program was adopted as part of the Temporary Liquidity Guarantee Program ("TLGP") to "stabilize" transaction accounts such as "payment-processing "accounts in order to offer relief to businesses, including lawyers and law firms, who otherwise might feel compelled to move those accounts from smaller, local banks and relocate them to banks considered "too big to fail" or to open multiple smaller accounts at different banks to maximize insurance coverage for their client funds.

The examples of IOLTA transactions cited above illustrate that IOLTA accounts are the very type of business transaction accounts intended for protection under the TAG Program. They also demonstrate that absent full IOLTA account coverage for individual client funds that exceed the $250,000 insurance limitation, lawyers are put in the untenable position of moving their IOLTA accounts to a large "safe" bank or attempting to split up a client's funds among multiple banks to obtain full coverage in an interest-bearing IOLTA account Using multiple banks to obtain full coverage, however, is not viable as many IOLTA deposits simply involve waiting for disbursement checks to clear. If a deposit is held just long enough to clear the banking system, it is not practical to require lawyers or law firms to first divide the funds among several banks in order to fully insure their clients' funds.

Also, as noted above, it is only because there is a non-profit interest beneficiary that interest can be paid on IOLTA accounts at all. Clients whose funds are deposited have no expectation of interest; to them, the account operates as a noninterest-bearing checking account. Lawyers (who are the account holders) are ethically prohibited from receiving any interest earned by client funds. Indeed, the only funds allowed to be deposited in IOLTA accounts are those that, as a practical matter, could not net any income for clients in excess of the costs of securing that income.[2] Additionally, FDIC action to include IOLTA accounts in the TAG Program full coverage guarantee would not pose further administrative burdens on participating banks or the FDIC in the event of a claim.[3]

While the question of whether IOLTA accounts are "noninterest-bearing deposit accounts" is not expressly addressed by the TLGP regulations, both the Federal Reserve and the FDIC have for other purposes (i.e. addressing the Regulation D prohibition on paying interest on demand accounts) determined that IOLTA accounts should be treated the same as noninterest-bearing accounts. We at NAIP see no reason why IOLTA accounts should be treated differently for purposes of the TAG Program than they are for purposes of Regulation D.

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2 See IRS Rev Ruling 87-2 holding that IOLTA interest is not includable in the gross income of either the client or law firm. Further, neither the bank holding IOLTA accounts nor the law firm participating in the program is required to report payment of interest under Section 6049 of the Code.

3 (1) The accounts already are labeled as "lawyer trust accounts." (2) The accounts carry the Tax I.D. of an IOLTA program and can be identified easily. (3) Attorneys are already required by their regulatory bodies to keep records so that individual fund owners can be identified.

Effects of Failure to Extend TAG Program to IOLTA Accounts.

There will be no benefit to the banking system or to the FDIC if the FDIC does not extend the benefits of the TAG Program to IOLTA accounts On the other hand, the FDIC's failure to extend the benefits of the TAG Program to IOLTA accounts would be devastating to IOLTA programs since many lawyers may feel compelled to move trust monies in excess of $250,000 per client from IOLTA accounts to noninterest-bearing accounts to qualify for the TAG Program. IOLTA accounts generate millions of dollars every year in grants to support legal aid to the poor and other law-related charitable projects such as educating lay people about the law and the legal system and are the second largest source of legal services funding in the country. Without IOLTA funding, legal aid organizations would be severely limited in providing civil legal assistance to poor individuals and families who cannot afford to hire a lawyer. Applying the TAG Program's unlimited insurance to IOLTA accounts would not only work toward the overarching goal of the TLGP to stabilize such accounts, but would ensure that client deposits remain in IOLTA accounts and continue to generate interest for these important charitable, public purposes.

We urge you to acknowledge that IOLTA accounts are covered by the TAG Program or to extend the TAG Program to IOLTA accounts. As noted above, there is ample basis on which to interpret the TLGP objectives as already including IOLTA accounts in the TAG Program's full coverage because IOLTA accounts are effectively the same as the transaction accounts identified in the regulation and have been recognized as such by the Federal Reserve Board and the FDIC in other contexts. Alternatively, an exception or amendment to the Interim Rule explicitly covering IOLTA accounts is warranted because excluding IOLTA accounts from full coverage would destabilize these accounts and cause the flight of deposits the TLGP seeks to prevent if lawyers are forced to abandon local banking relationships in favor of the perceived safety of larger institutions. Also, failing to extend full coverage to IOLTA accounts will cause funds to be moved from IOLTA accounts to noninterest-bearing accounts, undermining the important charitable purposes for which the Federal Reserve Board previously authorized IOLTA interest through NOW accounts. Severely reduced IOLTA interest would result in great harm to many indigent families with no place to go for help with critical civil legal needs.

We appreciate the opportunity to provide these comments and would be happy to provide further information upon request.

Sincerely,

Susan Erlichman
President,
National Association of IOLTA Programs

Enc: IOLTA Federal Reserve Determination Letters for Michigan, Maryland and New Jersey

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL BRADFIELD
GENERAL COUNSEL

September 11, 1987

Mr. Charles R. Rutherford
President
Michigan State Bar Foundation
306 Townsend Street
Lansing, Michigan 48933

Dear Mr. Rutherford:

This is in response to your letter requesting an opinion with regard to whether attorney trust funds may be deposited in interest bearing negotiable order of withdrawal ("NOW") accounts at member banks when such funds are maintained under the Interest on Lawyer Trust Account ("IOLTA") Program established by Administrative Order 1987-3 of the Michigan Supreme Court. Under the order, attorneys entrusted with clients' funds may commingle these funds into interest bearing accounts at depository institutions with the interest earned on these accounts to be remitted by the depository institution, at least quarterly, to the Michigan State Bar Foundation ("Foundation"). The Foundation will use the interest paid to it exclusively for charitable, religious, scientific or educational purposes; to be allocated as follows: not less than 80 percent to support the delivery of civil legal services to the poor; and not more than 20 percent to promote improvements in the administration of justice, advance the science of jurisprudence, and preserve the American constitutional form of government.

Section 303 of the Consumer Checking Account Equity Act of 1980 (Title III of P.L. 96-221) provides the following test of eligibility for maintaining NOW accounts: (1) the account must consist solely of funds in which the entire beneficial interest is held by one or more individuals, by a governmental unit, or by an organization operated primarily for religious, philanthropic, charitable, educational, or other similar purposes; and (2) the organization must not be operated for profit. (12 U.S.C. § 1832(a)). The Board regards this provision as including organizations not operated for profit that are described in section 501(c)(3) of the Internal Revenue Code (26 U.S.C. (I.R.C. 1954) § 501(c)(3)) (12 C.F.R. § 217.157).

In determining whether client funds may be deposited in NOW accounts under IOLTA programs similar to the Michigan program, the Board's Legal Division has required evidence that the organization administering the program is a nonprofit organization operated for "religious, philanthropic, charitable, educational, or other similar purposes" eligible for tax exempt status under section 501(c)(3) of the Internal Revenue Code. The Legal Division also requests an opinion from the State Attorney General that the organization involved holds the beneficial interest in the accounts involved because it has the exclusive right to the interest on the funds maintained in the program. Your letter and an enclosed copy of the Supreme Court order dated March 16, 1987 (with amendments), indicate that the Michigan program was established by that order, which, as amended, permits lawyers to establish interest-bearing trust accounts for clients' funds that are not expected to earn more than $50 in interest during the period it is anticipated such funds are to be held. All of the interest earned on the funds in the trust accounts is to be paid to the Michigan State Bar Foundation. The Foundation continues to be a tax-exempt organization qualified under section 501(c)(3) of the Internal Revenue Code as indicated by letter dated June 18, 1982.

You enclosed a letter dated September 2, 1987, from the Attorney General of Michigan, which concludes that the Michigan Bar Foundation will own the entire beneficial interest in and will have exclusive right to all the interest income earned on trust accounts established in conformance with DR 9-102(c)(1). Based on the ruling granting tax-exempt status as a 501(c)(3) organization, the Michigan Supreme Court order, and the opinion of the Attorney General of Michigan, it is my view that the Michigan State Bar Foundation has the necessary beneficial interest in the accounts since it holds the exclusive right to the interest earned on these accounts.

It is therefore my opinion that funds deposited pursuant to the IOLTA program established by the Michigan Supreme Court, may be deposited in NOW accounts at member banks of the Federal Reserve System.

Sincerely,

Michael Bradfield

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

OFFICE OF THE GENERAL COUNSEL

January 10, 1983

Charles B. Schelberg, Esq.
Miles & Stockbridge
10 Light Street
Baltimore, Maryland 21202

Dear Mr. Schelberg:

This is in response to your request, made on behalf of the Maryland State Bar Association, Inc., for an opinion with respect to whether Maryland attorneys may deposit client trust funds in negotiable order of withdrawal ("NOW") accounts at member banks, the interest on which is to be paid to the Maryland Legal Services Corporation (the "Corporation").

In reviewing programs similar to that authorized in 1982 by the Maryland General Assembly (1982 Md. Laws 829; Md. Ann. Code art. 10 §§ 45A to 450 (1982)), I have previously taken the position that the funds in question could be maintained in NOW accounts if certain conditions are satisfied. These conditions require (1) submissions expressing the view that the organization similar to the Corporation is a nonprofit organization organized for "religious, philanthropic, charitable, educational or other similar purposes" that qualifies under section 501(c)(3) of the Internal Revenue Code, and (2) an opinion rendered by the Attorney General of the state in question that the organization in question holds the beneficial interest in the accounts of those participating in the program because the organization has the exclusive right to the interest on the trust funds maintained under the program.

With respect to the program authorized under Maryland law, it is my opinion that the submissions included with your request fulfill these conditions. These submissions provide evidence that the Corporation is a nonprofit organization that qualifies under section 501(c)(3) of the Internal Revenue Code and an opinion rendered by the Maryland Attorney General expressing the view that the Corporation has the exclusive right to interest earned on the trust accounts. Consequently, it is my opinion that funds deposited under this program may be maintained in NOW accounts.

I should note, however, that the Board recently amended Regulation Q--Interest on Deposits (12 C.F.R. § 217) to provide that governmental units are eligible to maintain NOW accounts at member banks. I have enclosed a copy of the Board's official notice in this matter for your information. As a result of this action, the first condition could also be met by submissions expressing the view that the Corporation is a governmental unit.

I hope that this is of assistance to you.

Sincerely,

Michael Bradfield

Michael Bradfield
General Counsel

Enclosure

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL BRADFIELD
GENERAL COUNSEL

MAY 11 1988

Mr. Joel A. Kobert
Chair, IOLTA Board of Trustees
The IOLTA Fund of the Bar of New Jersey
New Jersey Law Center
One Constitution Square
New Brunswick, New Jersey 08901-1500

Dear Mr. Kobert:

This is in response to your letter requesting an opinion with regard to whether attorney trust funds may be deposited in interest bearing negotiable order of withdrawal ("NOW") accounts at member banks when such funds are maintained under the Interest on Lawyer Trust Account ("IOLTA") Program established pursuant to amended rules of the New Jersey Supreme Court. Under New Jersey Supreme Court Rule 1:28-A, attorneys shall deposit all clients' funds into interest bearing accounts at insured depository institutions in New Jersey with the interest earned on these accounts to be remitted to the IOLTA Fund of the Bar of New Jersey ("Fund") by the depository institution. The Fund will use the interest paid to it exclusively for charitable, religious, scientific or educational purposes; but primarily to make grants for (i) legal aid to the poor, (ii) improvement of the administration of justice, (iii) education of lay persons in legal and justice related areas, or (iv) such other programs to benefit the public as are approved by the Supreme Court of New Jersey.

Section 303 of the Consumer Checking Account Equity Act of 1980 (Title III of P.L. 96-221) provides the following test of eligibility for maintaining NOW accounts: (1) the account must consist solely of funds in which the entire beneficial interest is held by one or more individuals, by a governmental unit, or by an organization operated primarily for religious, philanthropic, charitable, educational, or other similar purposes; and (2) the organization must not be operated for profit. (12 U.S.C. § 1832(a)). The Board regards this provision as including organizations not operated for profit that are described in section 501(c)(3) of the Internal Revenue Code (26 U.S.C. (I.R.C. 1954) § 501(c)(3)) (12 C.F.R. § 217.157).

In determining whether client funds may be deposited in NOW accounts under IOLTA programs similar to the New Jersey program, the Board's Legal Division has required evidence that the organization administering the program is either a governmental unit or a nonprofit organization operated for "religious, philanthropic, charitable, educational, or other similar purposes" eligible for tax exempt status under section 501(c)(3) of the Internal Revenue Code. The Legal Division also requests an opinion from the State Attorney General that the organization involved holds the beneficial interest in the accounts involved because it has the exclusive right to the interest on the funds maintained in the program. Your letter and an enclosed copy of the New Jersey Supreme Court rule indicate that the New Jersey program was established by the New Jersey Supreme Court by its Rule 1:28-A. This rule requires lawyers to establish interest-bearing trust accounts for clients' funds that are nominal in amount or are expected to be held for a short period of time. All of the interest earned on the aggregate nominal funds in the trust accounts is to be owned by the Fund.

I find that an Attorney General's opinion is unnecessary because the New Jersey Supreme Court Rule 1:28-A states that the Fund will be the owner of any interest generated by the funds deposited in an IOLTA interest-bearing trust account. Based on this Rule, it is my view that the New Jersey IOLTA Fund holds the exclusive right to the interest earned on these accounts.

You have stated in your letter that the Fund is a creation of the New Jersey Supreme Court, which also appoints the Board of Trustees who govern the Fund. Thus, you assert, the Fund is an arm of the State of New Jersey. Based on this assertion, I find that the Fund is eligible to hold a beneficial interest in a NOW account as a governmental unit.

It is therefore my opinion that funds deposited pursuant to the IOLTA program established by New Jersey Supreme Court Rule 1:28-A, may be deposited in NOW accounts at member banks of the Federal Reserve System.

Sincerely,

Michael Bradfield