



# SOLICITORS' ACCOUNT

SQE 1 PREP

LAW ANGELS

## **SOLICITORS'ACCOUNT**

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# PREFACE

The management of client money is not merely an administrative task; it is a fundamental pillar of professional integrity and trust in the legal profession. The *Solicitors Accounts Rules* (SAR) form a detailed and uncompromising framework designed to protect client funds and maintain the highest standards of financial probity. This textbook is designed to be your clear and practical guide through this essential, yet often daunting, aspect of legal practice.

Our approach is built on a simple belief: to master solicitors' accounts, you must understand the underlying principles, not just memorise the rules. We have therefore structured this text to demystify the SAR, breaking down complex requirements into logical, manageable components. Each chapter focuses on a key area of practice, from receiving client money and making payments from the client account to managing office money and performing the three-way reconciliation, illustrating the rules with clear examples and common scenarios.

The SQE1 assessment and your future practice require a precise and application-based knowledge. This book is tailored to that challenge. We present the SAR not as a list of prohibitions, but as a positive framework for effective financial management. Worked examples, ledger entries, and case studies based on typical transactions are woven throughout to transform abstract rules into practical competence.

Our goal is to equip you with the confidence and precision to handle client money correctly from day one. The following pages will provide the clarity, procedural knowledge, and ethical grounding you need to navigate this critical area with assurance, ensuring you uphold the trust that is the foundation of our profession.

Welcome to the study of solicitors' accounts. While the detail is exacting, there is no more important skill for safeguarding your reputation and that of the profession.

*Law Angels*

# ACKNOWLEDGEMENTS

The development of this textbook was a significant endeavor, and we extend our sincere gratitude to the collective efforts that made this publication possible.

At Law Angels, we are fortunate to be supported by a dedicated team whose commitment to legal education and excellence is the cornerstone of our work. The collaborative spirit, legal expertise, and tireless effort of our entire organization were instrumental in shaping this text from concept to completion.

We also extend our appreciation to the broader legal community. The insightful feedback from our academic and practitioner reviewers greatly enhanced the accuracy and clarity of the material. Their contributions, offered in a spirit of scholarly collaboration, have been invaluable in ensuring this resource meets the rigorous demands of the SQE curriculum.

We are also thankful for the unwavering support from our personal networks, whose understanding provided the foundation that allowed this project to thrive.

It is our privilege at Law Angels to contribute to the education of future solicitors, and we hope this text serves as a reliable guide for the next generation of legal professionals.

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3. Solicitors Regulation Authority (SRA) Accounts Rules 2019
4. UK General Data Protection Regulation

# GLOSSARY OF KEY TERMS

This glossary defines the key terms used in this textbook and in the SRA Accounts Rules. Understanding this language is the first step to mastering solicitors' accounts.

## A

**Accountant's Report:** A formal report prepared by a qualified accountant. It is required for most firms that hold or receive client money and provides an independent opinion to the SRA on whether the firm has complied with the Accounts Rules during the reporting period.

## B

**Bank Reconciliation:** The process of comparing the firm's own financial records (the cash book) for a client or office bank account with the corresponding bank statement. The balances must match, and any differences (e.g., unpresented cheques) must be explained and documented.

**Bill of Costs:** An itemised claim submitted to a client or another party for payment of the solicitor's professional fees and disbursements.

**Breach of the Accounts Rules:** Any failure to comply with the SRA Accounts Rules. Upon discovery, a breach must be corrected immediately, and serious breaches must be reported to the SRA.

## C

**Client Account:** A current or deposit account at a bank or building society, used only to hold client money. The account name must include the name of the firm and the word "client" to distinguish it from the office account.

**Client Account Reconciliation:** A mandatory monthly process to ensure the integrity of the accounting records. It involves checking that the balance on the client bank statement agrees with the total of the balances shown on all the individual client ledgers.

**Client Ledger:** A detailed record for each individual client (or matter) showing all the financial transactions related to them, such as money received, money paid out, and transfers. The total of all client ledger balances must always equal the balance on the client bank account.

**Client Money:** Money held or received by a firm that is not the firm's money. This includes money held for a client, as a trustee, as an agent, or as a stakeholder. It is the core concept of the Accounts Rules.

## D

**Disbursement:** A payment made by the firm on behalf of a client. There are two types:

- **Agency Disbursement:** A payment to a third party where the firm is acting as the client's agent (e.g., a court fee, search fee, or barrister's fee). The firm acts as a mere channel for the client's money.
- **Principal Disbursement:** A payment to a third party that is reclaimed as part of the firm's costs (e.g., photocopying, travel, or postage). These are treated as costs of the firm from the outset.

## E

**Office Account:** A bank account used for holding all money belonging to the firm, such as profits, capital, and payments received from clients for bills that have been delivered.

## I

**Interest:** The sum payable by a firm to a client for the use of their money held in a client account. The SRA Accounts Rules set out when this duty arises and the minimum calculation method that must be used.

**L**

**Lien:** A right to retain possession of property belonging to another person until a debt is paid. In the context of accounts, a solicitor may have a lien over client money or documents for their unpaid costs, which is a permitted reason to withhold client money from a client account.

**M**

**Money Belonging to the Firm:** All money that is not client money. This includes the firm's profit, capital, and money received from a client in payment of a properly delivered bill.

**R**

**Reconciliation:** See Bank Reconciliation and Client Account Reconciliation.

**Right to Retain:** See Lien.

**S**

**SRA Accounts Rules:** The set of rules issued by the Solicitors Regulation Authority that govern how solicitors and law firms in England and Wales must handle client money. Compliance is a mandatory condition of practice.

**T**

**Third-Party Managed Account (TPMA):** An account where the money is held by a third party (not the firm or the client) but the firm has some authority to instruct transactions on it. The use of TPMAs can, in certain circumstances, mean the money is not classified as "client money" for the purposes of the SRA Accounts Rules.

**Transfer:** The movement of money from one part of the accounting system to another. Key types include transferring money from the client account to the office account upon payment of a bill, or transferring money between two client ledgers.

**V**

**VAT (Value Added Tax):** A tax on goods and services. In a legal context, VAT is typically added to bills of costs (on fees and some disbursements) and must be properly accounted for and paid to HM Revenue & Customs.



# 1

## INTRODUCTION TO SOLICITORS' ACCOUNT AND THE REGULATORY FRAMEWORK

The management of client money is a fundamental aspect of legal practice and a core expression of the solicitor's fiduciary duty. It reflects the profession's ethical commitment to act in the client's best interests, maintain strict financial integrity, and safeguard public confidence in the legal system. The *Solicitors Regulation Authority (SRA) Accounts Rules 2019* provide the principal framework governing this duty, requiring client funds to be protected, kept distinct from the firm's own money, and applied solely for authorised purposes. These obligations apply not only to firms as entities but also personally to managers, employees, and compliance officers, ensuring accountability at every level of legal practice.

In addition to regulatory compliance, solicitors must also possess a working understanding of financial principles such as double-entry bookkeeping and the correct application of debits and credits. These principles underpin accurate record-keeping and transparent accounting, enabling firms to demonstrate proper stewardship of client assets. Together, the regulatory framework and accounting fundamentals establish a system designed to prevent misuse of funds, promote professional responsibility, and sustain the trust on which the solicitor–client relationship depends.

### **1.1 The Fundamental Duty of Stewardship and Fiduciary Responsibility**

Imagine your friend gives you £500 to hold onto so you can buy a concert ticket for them. That money isn't yours. You can't spend it on a new video game. You have a responsibility to keep it safe and use it only for its intended purpose. This is a simple form of stewardship.

Now, amplify that by millions of pounds, and you have the world of a solicitor. Clients trust law firms with their money for house deposits, divorce settlements, and business deals. This trust is the foundation of the legal profession.

As a solicitor, you are a fiduciary. This is a legal and ethical duty to act in the best interests of your client, putting their interests ahead of your own. When it comes to client money, this means:

- It must be safe.
- It must be separate from the firm's money.
- It must only be used for the client's specific matter.

This duty of stewardship and fiduciary responsibility is the "why" behind all the rules you will learn.

## **1.2 Overview and Purpose of the *SRA Accounts Rules 2019***

The Solicitors Regulation Authority (SRA) is the regulator for solicitors in England and Wales. To ensure all firms meet their fiduciary duties, the SRA created the SRA Accounts Rules.

Think of these Rules as the official instruction manual for handling client money. The current version came into effect in November 2019.

The main purposes of the Rules are:

1. The number one goal is to keep client money safe.
2. To maintain public trust; people must be able to trust solicitors without question.
3. The Rules provide a clear framework; they tell you what you must do, even if they don't always spell out exactly how to do it.

The *2019 Rules* are more principles-based than older, more rigid versions. This means they focus on the key outcomes (e.g., "keep client money safe") and allow firms to design their own systems to achieve them, rather than following hundreds of tiny, prescriptive commands.

### 1.3 Who is Bound by the Rules?

The *Rules* don't just apply to the "firm" as a vague entity. The obligation is personal and wide reaching. According to the *Rules*, "you" must comply, and "you" means:

1. **The authorised body:** This is the law firm itself (whether it's a sole practice, partnership, or LLP).
2. **Managers:** This includes partners, members of an LLP, and directors of a recognised body.
3. **Employees:** This means everyone who works at the firm, including solicitors, paralegals, and cashiers.

Crucially, managers are jointly responsible for ensuring everyone in the firm complies. You cannot claim you didn't know what was happening; the duty is on you to ensure proper systems are in place and followed.

### 1.4 The Principles-Based Approach vs. Prescriptive Rules

The difference in approach is illustrated below.

- **Prescriptive rule (Old school):** "You must pay a client cheque into the client account within 2 working days of receipt."
- **Principles-Based Rule (Current):** "You must pay client money into a client account promptly."

The principles-based approach uses words like "promptly" and "fair." This gives firms flexibility but also requires them to use their professional judgment. What is "prompt" for a large commercial firm with instant banking might be different for a small high-street practice,

but in both cases, the firm must be able to justify its actions as being in the client's best interests.

## 1.5 Consequences of Non-Compliance

Getting the accounts wrong is serious. The consequences can be:

### Regulatory

Non-compliance with the *SRA Accounts Rules* can lead to investigations, disciplinary hearings, and sanctions by the SRA. Penalties range from fines on the individual or firm and practising restrictions to suspension or being struck off the roll (meaning they can no longer practise), particularly where dishonesty is involved. Such outcomes can irreparably damage a solicitor's career and professional reputation.

### Civil

A breach of accounting obligations may expose the firm to civil liability if a client suffers financial loss or a breach of contract occurs. Clients can sue to recover misused or lost funds, and the resulting damages and legal costs can significantly affect the firm's financial stability. Civil claims may also harm client relationships and public trust.

### Criminal

In the most serious cases, such as theft, fraud, or deliberate misuse of client funds, non-compliance can amount to a criminal offence. Conviction may result in prosecution, fines, and imprisonment, alongside lasting reputational damage. Such outcomes often end a solicitor's ability to practise and undermine confidence in the profession.

**Example:** A solicitor uses £5,000 of Client A's money to pay a bill for Client B, intending to replace it when another cheque comes in. Even with no dishonest intent, this is a serious breach. The SRA would likely take disciplinary action, and if the firm became insolvent before the money was replaced, Client A would have suffered a direct loss.

## 1.6 The Role of the Compliance Officer for Finance and Administration

Every firm must appoint a Compliance Officer for Finance and Administration (COFA). The COFA is the person responsible for ensuring the firm complies with the Accounts Rules. They are the SRA's main contact for accounts matters.

The COFA's job is to monitor the firm's compliance, report any serious breaches to the SRA, and ensure proper accounting systems are in place.

The COFA doesn't have to do all the bookkeeping, but they must have oversight and authority.

## 1.7 Introduction to Double-Entry Bookkeeping: The Accounting Equation

All law firms (and indeed, most businesses) use a system called double-entry bookkeeping. It sounds complicated, but the core idea is simple: every transaction has two sides.

The system is built on a fundamental formula known as the Accounting Equation:

$$\text{Assets} = \text{Liabilities} + \text{Equity}$$

Where:

- Assets mean what the business OWNS (e.g., cash, buildings, computers).
- Liabilities mean what the business OWES to others (e.g., bank loans, unpaid bills).
- Equity means the owner's stake in the business.

This equation must always balance.

**Example:** Your firm buys a new £1,000 computer.

- The firm gains an Asset (the computer, worth £1,000). The firm loses another Asset (cash in the bank, worth £1,000).
- The equation remains in balance because one asset increases and another decreases by the same amount.

## 1.8 Debits and Credits: The REAL Story (Forget Everything You Think You Know!)

You're right. In everyday life, a "debit" on your bank statement means money left your account, and a "credit" means money came in.

However, in accounting, and especially in solicitors' accounts, WE FORGET THAT MEANING COMPLETELY.

Here, Debit (Dr) and Credit (Cr) do NOT mean "good/bad" or "in/out." They are simply technical terms for LEFT and RIGHT.

Think of it like a game of seesaw. For the seesaw to be balanced, whatever happens on one side must be matched on the other side.

### 1.8.1 The Secret Code: What Debits and Credits Actually Do

Let's look at the four main types of accounts in a law firm and what a Debit or Credit does to them.

Type of Account	A DEBIT (Left) does this:	A CREDIT (Right) does this:
Asset (Something the firm OWNS)  e.g., Bank Account, Office Furniture	INCREASES the Asset	DECREASES the Asset
Liability (Something the firm OWES)  e.g., Bank Loan, Bill from a supplier	DECREASES the Liability	INCREASES the Liability

Income (Money the firm EARNs) e.g., Profit Costs	DECREASES the Income	INCREASES the Income
Expense (Money the firm SPENDs) e.g., Rent, Salaries	INCREASES the Expense	DECREASES the Expense

This might seem backwards now, but it's the rule. Let's bring it to life.

### Let's Play a Game: "Spot the Debit and Credit"

We'll follow one golden rule: For every transaction, one account gets a DEBIT and another gets a CREDIT, and the amounts must be equal.

#### Example 1: The Firm Buys a Computer for £1,000 Cash

What's happening?

1. The firm is gaining an Asset (the computer).
2. The firm is losing another Asset (cash from its bank account).

Let's apply the code:

- Gaining an Asset? That's an INCREASE. To increase an Asset, we DEBIT the "Office Equipment" account.
- Losing an Asset? That's a DECREASE. To decrease an Asset, we CREDIT the "Cash/Bank" account.

The Double Entry is:

- DEBIT Office Equipment £1,000
- CREDIT Bank £1,000

The seesaw is balanced!

### **Example 2: The Firm Pays its £500 Electricity Bill**

What's happening?

1. The firm is increasing an Expense (the cost of electricity).
2. The firm is decreasing an Asset (cash).

Apply the code:

- Increasing an Expense? To increase an Expense, we DEBIT the "Electricity" account.
- Decreasing an Asset? To decrease an Asset, we CREDIT the "Bank" account.

The Double Entry is:

- DEBIT Electricity Expense £500
- CREDIT Bank £500

The seesaw is balanced again!

### **Example 3: The Firm Sends a Bill to a Client for £2,000**

This is a tricky one because no cash has moved yet! But the firm has *earned* the right to that money.

What's happening?

1. The firm has increased its Income (it has earned £2,000 in fees).
2. The firm has gained a new Asset (the client now owes the firm £2,000 - this is a debt, which is an asset called "Debtor").

Apply the code:

- Increasing Income? To increase Income, we CREDIT the "Profit Costs" account.



- Gaining an Asset (a Debtor)? To increase an Asset, we DEBIT the "Client Debtor" account.

The Double Entry is:

- DEBIT Client Debtor £2,000
- CREDIT Profit Costs £2,000

See? No cash was involved, but the double entry still works!

### **The Super-Important Twist: Client Money**

Now, let's apply this to the most important part: the Client Bank Account.

The Client Bank Account is an Asset for the firm, but it's a very special one. The money in it doesn't belong to the firm; the firm is just looking after it. Because of this, we also have to track the firm's Liability (what it OWES) to each individual client.

Let's see how this works.

### **Example 4: A Client Gives You £5,000 "On Account" of Costs**

What's happening?

1. The firm's Client Bank Account (an Asset) increases by £5,000.
2. The firm's obligation to the client (a Liability) increases by £5,000.

Apply the code:

- Increasing an Asset (Client Bank Account)? We DEBIT the Client Bank Account.
- Increasing a Liability (Money owed to the client)? We CREDIT the client's personal ledger account.

The Double Entry is:

- DEBIT Client Bank Account £5,000
- CREDIT Client Ledger Account £5,000

This shows the firm is holding £5,000 *for* the client.

### **Example 5: You Pay a £400 Search Fee for the Client from the Client Account**

What's happening?

1. The firm's Client Bank Account (an Asset) decreases by £400.
2. The firm's obligation to the client (a Liability) decreases by £400 (because you've used their money for its intended purpose).

Apply the code:

- Decreasing an Asset (Client Bank Account)? We CREDIT the Client Bank Account.
- Decreasing a Liability (Money owed to the client)? We DEBIT the client's personal ledger account.

The Double Entry is:

- DEBIT Client Ledger Account £400
- CREDIT Client Bank Account £400

This shows the firm now only holds £4,600 for the client.

### **The Ultimate Cheat Sheet**

To make it stick, remember this simple phrase:

"Debit the receiver, Credit the giver."

- In Example 1: Debit the receiver of the computer, Credit the giver of the cash (the bank).
- In Example 4: Debit the receiver of the cash (the Client Bank Account), Credit the giver (the client).
- In Example 5: Debit the receiver of the payment (the search company, via the client ledger), Credit the giver of the cash (the Client Bank Account).

It's not a perfect rule for every single scenario, but it's a fantastic starting point to build your understanding. Stop thinking of Debit and Credit as "in and out," and start thinking of them as "left and right" that must always, always balance.

## 1.9 The Chart of Accounts for a Legal Practice

A Chart of Accounts is a list of all the accounts a firm uses to record its transactions, like a table of contents for the finances. For a law firm, this is split into two main sets:

1. **Client accounts:** For tracking money held for clients (e.g., "Client Bank Account," "Client A Matter X Ledger").
2. **Business (or Office) accounts:** For tracking the firm's own money (e.g., "Office Bank Account," "Profit Costs," "Rent Expense," "HMRC VAT").

The golden rule is never mix the entries between these two sets. A debit in a client account must be matched with a credit in another client account (or the client cash account), never with a credit in a business account.

## 1.10 Case Studies: Common Failings and How to Avoid Them

### Case Study 1: The "Helpful" Transfer

#### Scenario

A client, after selling her house, asks her solicitor to pay her son's university fees directly from the sale proceeds held in the client account. The solicitor agrees to be helpful.

**The Breach:** This is an improper use of the client account as a banking facility (*Rule 3.3*). The payment has no connection to the legal transaction (the house sale). The client should receive the funds and pay the fees herself.

**How to Avoid:** Only make payments from client account that are directly related to the legal service you are providing. Politely explain to the client why you cannot act as their general bank.

## Case Study 2: The Overdrawn Client Ledger

### Scenario

A solicitor holds £1,000 for Client B. He needs to pay a £1,200 court fee for Client B. He pays the full £1,200 from the client account, thinking he'll sort it out later.

**The Breach:** This is a breach of *Rule 5.3*. The solicitor has used £200 that belongs to other clients. This is a very serious breach, even if no money is ultimately lost.

**How to Avoid:** Never withdraw more money for a client than is held for them. If there are insufficient funds, the payment must be made from the firm's business account, creating a debt the client owes the firm.

## Case Study 3: The Delayed Deposit

### Scenario

A firm receives a large cheque for a client's property purchase on a Friday. The cashier puts it in a drawer and doesn't pay it into the client account until the following Tuesday.

**The Breach:** This is a failure to pay client money into a client account promptly (*Rule 2.3*). The client's money was at risk and not earning interest.

**How to Avoid:** Have a clear, strict policy. In the age of online banking, "promptly" often means the same day.

## 1.11 Conclusion

The regulation of solicitors' accounts is central to maintaining the integrity of legal practice and the confidence of clients in the profession. Through the *SRA Accounts Rules*, solicitors are held to stringent standards of transparency, accuracy, and separation of client and office money. Compliance with these standards not only fulfils legal and ethical obligations but also protects firms from significant regulatory, civil, and criminal consequences that can arise from mismanagement or misuse of client funds.

Ultimately, the careful management of client money is more than a procedural requirement; it is a reflection of the solicitor's professional character and ethical standing. A clear understanding of both regulatory duties and financial principles enables solicitors to discharge their responsibilities effectively, uphold public trust, and contribute to the proper administration of justice.

# 2

## CLIENT MONEY

The proper handling of client money lies at the heart of professional conduct within legal practice. The *Solicitors Regulation Authority (SRA) Accounts Rules 2019* define client money with precision, ensuring that funds entrusted to solicitors—whether for services, as stakeholder holdings, or in fiduciary capacities—are protected and clearly distinguished from the firm's own assets. This demarcation preserves the fiduciary duty owed by solicitors to their clients and reinforces public trust in the profession. Compliance with these rules ensures that solicitors act as responsible custodians, maintaining transparency, accountability, and integrity in financial dealings.

This chapter explores the various forms and classifications of client money, the mandatory requirement for prompt deposit into a client account, and the limited circumstances under which withholding is permissible. It further examines practical accounting entries and case-based applications to strengthen understanding of how these principles operate in day-to-day legal practice. The overarching aim is to provide both conceptual clarity and procedural precision, enabling solicitors to manage client funds ethically, lawfully, and with the diligence expected of their fiduciary position.

### 2.1 The Statutory Definition of Client Money

Think of Client Money as a special box labelled "Other People's Property." The *SRA Accounts Rules* give us a very specific list of what must go into this box. According to the *Rules*, Client Money is any money you hold or receive in the course of your practice that is:

1. (a) For regulated services you are providing to a client.

2. (b) On behalf of a third party in relation to your services (e.g., money held as an agent, or as a stakeholder).
3. (c) As a trustee, attorney under a power of attorney, or other specified office.
4. (d) In respect of your fees and any unpaid disbursements, if you get the money before you've sent the client a bill.

### **The Golden Rule**

If money fits any of these descriptions, it is Client Money and must be treated with the highest level of care. If it doesn't fit, it's the firm's own money (often called "Office Money" or "Business Money").

## **2.2 Money You Hold for a Client: Receipts for Services, Damages, Property Sales**

This is the most straightforward category. It is money that belongs to the client and is given to you to use for their matter.

Examples include:

- A client gives you £1,000 "on account of costs" to cover future work and expenses. (This is client money under (d) above until you bill for it).
- You receive a £50,000 cheque from a buyer for your client's house purchase. (This is client money under (a) above).
- You win a litigation case and the other side pays £20,000 in damages into your firm's account. (This is client money under (a) above).

In all these cases, you are the guardian of this money. It is not yours to use for any other purpose.

## **2.3 Money You Hold as Stakeholder: The Enhanced Obligations**

Holding money as a stakeholder is like being a referee holding the prize money. You don't hold it for one person; you hold it for both parties to a transaction, and you can only release it when certain conditions are met.

### **The Classic Example: A Property Deposit**

When you act for a seller, the buyer's solicitor will send you a 10% deposit on the property. The contract usually states this is held as "stakeholder." This means:

- You are holding it for the buyer and the seller jointly.
- It does not belong to your client (the seller) until the moment the sale is completed.
- If the sale falls through through the buyer's fault, you may need to return it to the buyer.  
If it falls through through the seller's fault, you may need to pay it to the buyer.

Your obligation is one of strict neutrality. You cannot release this money to your client until completion happens. This is a higher duty than simply holding money for your own client.

## **2.4 Money You Hold for a Third Party: Payments to Experts, Barristers, etc.**

Sometimes, you receive money that is meant for someone else, but you are the one handling it. This is still Client Money.

Examples include:

- A client gives you money to pay their barrister's (counsel's) fees.
- You receive funds from an opponent that are specifically meant to pay your client's medical expert.
- You hold money "to the sender's order", meaning the sender hasn't yet told you who it belongs to.



In these cases, you are not holding the money for your client, but for the third party (the barrister, the expert, etc.). You must keep it safe and pay it to the correct person when instructed or when the time is right.

## 2.5 The Absolute Requirement to Pay Client Money into a Client Account Without Delay

The most fundamental rule is that when you receive Client Money, you must pay it into a client bank account (an account with the word "client" in its title) PROMPTLY.

### Meaning of Promptly

The *Rules* don't give a specific number of days because technology changes. The key question is: "What is in the client's best interests to keep their money safe?"

- In the age of online banking, "promptly" often means the same day, or at the very latest, the next working day.
- Letting a cheque sit in a drawer for a week is a clear breach.

Why is this so important?

1. **Safety:** Money in the client account is protected. Money in a desk drawer or the firm's office account is not.
2. **Separation:** It ensures client money is never mixed with the firm's money.
3. **Trust:** It demonstrates you are acting properly.

## 2.6 Permissible Withholdings: The Limited Exceptions

There are only a few, very specific situations where you can legitimately keep Client Money out of the client account.

### **2.6.1 Money for an Agreed Disbursement (The "Paid Away" Rule)**

If you receive money from a client that is solely for a disbursement you have already paid, it is not Client Money.

**Example:** You paid a £300 court fee for your client from the firm's own money. The client now gives you a cheque for £300 to reimburse you. This cheque is Office Money from the moment you receive it. It must go straight into the office account because you have already spent the money.

### **2.6.2 Money for Your Costs: The Strict Conditions**

Money for your fees is Client Money until you have sent the client a bill. Once a bill is delivered, the money owed becomes a debt. If the client then pays that bill, the money is yours.

**Example:** You hold £1,000 of client money for Client X. You do £800 worth of work and send Client X a bill for £800. You can now transfer £800 from the client account to the office account. The remaining £200 is still client money.

### **2.6.3 Client Instruction to Hold Money Elsewhere (In Writing)**

A client can instruct you in writing not to put their money in a client account. However, you must be very careful here. You need to be sure the client understands the risks (their money won't have the same protections) and you must have a good reason for agreeing (e.g., the client is a sophisticated financial institution with its own treasury department). For most private clients, you should not agree to this.

### **2.6.4 Disputes over Entitlement: The Duty to Take Reasonable Steps**

If two people claim the same money (e.g., in a divorce, both spouses claim a fund), you cannot safely pay it to either one. You must:

1. Hold the money in the client account.
2. Take all reasonable steps to resolve the dispute (e.g., mediate, get a court order).
3. Only release the money once the dispute is settled.

Paying out without a resolution is highly risky.

## 2.7 The Process and Timing for Repaying Client Money to the Client

Just as you must pay client money into the client account promptly, you must pay it *out* to the client promptly when you no longer have a reason to hold it.

When should you return client money?

- At the end of a matter.
- When the client asks for it back.
- When you stop acting for the client.

**Example:** A client gives you £2,000 for a purchase that falls through. The client asks you to hold the money while they find a new property. After two months, they still haven't found one. The safest and most proper course is to return the money to them. Holding it for long periods with no active transaction could be a breach of the rules.

## 2.8 Accounting Entries for Receiving Client Money

Remember Debit and Credit from Chapter 1? Let's use them. When you receive Client Money, two things happen:

1. Your Client Bank Account (an Asset) increases.
2. Your obligation to the client (a Liability) increases.

Using our code:

- To increase an Asset, you DEBIT.
- To increase a Liability, you CREDIT.

The double entry for receiving any Client Money is always:

- DEBIT Client Bank Account
- CREDIT [Client Name] Ledger Account

## Illustration

Client Ahmed pays £5,000 on account of costs via bank transfer.

Client Bank Account			
Date	Details	Debit (Dr)	Credit (Cr)
01/10	Ahmed - on account	5,000	

Client: Ahmed	Business	Client		
Matter: Purchase				
Date	Details	Debit (Dr)	Credit (Cr)	Balance
01/10	Client Bank		5,000	5,000 Cr

This shows the firm's client account has £5,000 more in it, and the firm owes £5,000 to Ahmed.

## 2.9 Accounting Entries for Paying Client Money to the Client or Third Parties

When you pay money out of the client account, two things happen:

1. Your Client Bank Account (an Asset) decreases.
2. Your obligation to the client (a Liability) decreases.

Using our code:

- To decrease an Asset, you CREDIT.
- To decrease a Liability, you DEBIT.

The double entry for paying out Client Money is always:

- DEBIT [Client Name] Ledger Account
- CREDIT Client Bank Account

### Illustration

You pay a search fee of £250 for Client Ahmed from the client account.

Client Bank Account			
Date	Details	Debit (Dr)	Credit (Cr)
01/10	Ahmed - on account	5,000	
02/10	Search Co - for Ahmed		250

Client: Ahmed Matter: Purchase		Business	Client		
Date	Details	Debit (Dr)	Credit (Cr)	Balance	
01/10	Client Bank		5,000	5,000 Cr	
02/10	Search Co	250		4,750 Cr	

This shows the client account has £250 less, and the firm now only owes £4,750 to Ahmed.

## 2.10 Practical Exercise: Identifying Client Money in Complex Scenarios

### Scenario 1: The Mixed Cheque

You receive a cheque from a client for £150,500. The covering letter says: "£150,000 for the purchase completion, and £500 for your bill you sent last week."

£150,000: This is for the purchase. It is Client Money. It must be paid into the client account.

£500: This is in payment of a delivered bill. It is Office Money. It must be paid into the office account.

**Action:** Ideally, ask the client for two separate cheques. If you can't, pay the whole cheque into the client account and then immediately transfer £500 to the office account.

### Scenario 2: The Unexpected Windfall

You are administering an estate. A forgotten relative dies and leaves £10,000 directly to your firm (as named executor) for the estate.

Is this Client Money? Yes! You are holding it as a trustee (category (c) above). Even though it was paid directly to the firm, it belongs to the estate. It must be paid into the client account promptly.

### Scenario 3: The "Helpful" Payment

A client sells his business. After completion, he asks you to pay his daughter's £5,000 university fees directly from the sale proceeds still in your client account.

Is this allowed? NO! This is an improper use of the client account as a banking facility. The legal work (the sale) is over. The client should receive the money and pay the fees himself. Making this payment would be a serious breach of the *Rules*.

By working through these scenarios, you train your brain to automatically ask: "Who does this money belong to, and what is the proper thing to do with it?" This is the core of handling client money.

## 2.11 Conclusion

The management of client money embodies the solicitor's dual responsibility to the client and to the profession as a whole. The *SRA Accounts Rules* establish clear safeguards to ensure that client funds are received, held, and repaid in a manner consistent with both fiduciary and regulatory expectations. Adhering to these standards not only protects clients from financial loss but also upholds the credibility of the solicitor as a trusted intermediary in the legal process.

Ultimately, effective compliance with client money regulations reflects a solicitor's commitment to integrity and professional excellence. Whether handling stakeholder deposits, reimbursing disbursements, or maintaining accurate ledger entries, each action must demonstrate transparency and respect for client ownership. Through disciplined practice and ethical awareness, solicitors reinforce the trust that forms the foundation of their professional authority and the justice system itself.

# 3

## CLIENT ACCOUNT

The client account is the central mechanism through which solicitors uphold their fiduciary responsibility to safeguard client funds. More than a mere banking arrangement, it operates under a statutory trust, ensuring that money held belongs beneficially to the client and not to the firm. The *Solicitors Regulation Authority (SRA) Accounts Rules 2019* prescribe stringent requirements governing how such accounts are titled, maintained, and supervised, reflecting the legal profession's commitment to transparency, accountability, and the protection of client interests. This framework ensures that client money is ring-fenced, protected from the firm's liabilities, and managed solely for its intended legal purpose.

This chapter explores the legal nature and practical operation of the client account, from naming conventions and the use of authorised banks to the rules governing withdrawals, designated deposits, and prohibitions on using client accounts as banking facilities. It also examines how solicitors must apply proper authorisation, maintain dual control, and preserve an audit trail for every transaction. Through these provisions, the chapter highlights how sound accounting practices and regulatory compliance work together to maintain the profession's integrity and prevent the misuse of client funds.

### **3.1 Legal Meaning of a Client Account; the Statutory Trust**

Think of a client account not just as a bank account, but as a safeguard. Legally, it operates under a "statutory trust." This is a fancy term for a very simple, powerful idea:



When client money is in a client account, the law firm is the legal owner (its name is on the account), but it is not the beneficial owner. The firm is merely the trustee, holding the money on trust for the client, who is the beneficiary.

What does this mean in practice?

**The money is ring-fenced:** If the law firm goes bankrupt, the money in the client account is protected. It does not belong to the firm's creditors. It must be returned to the clients.

**Fiduciary duty:** The firm has the highest possible duty (a fiduciary duty) to manage the money solely in the client's interests.

**No mixing:** The firm's own money must not be mixed with client money in this account. It's like having a safe deposit box for each client's assets, all within one big vault.

### 3.2 Rules for Naming the Account: Clarity and Identification

You can't just name the account "Law Firm PLC Bank Account." The rules are specific to make sure everyone, especially the bank, knows what it is.

A client account must:

1. Be in the name of the firm (or the sole practitioner).
2. Include the word "client" in its title.

Examples include: "Smith & Jones LLP - Client Account", "A. Brown Solicitors - Client Account".

#### Why is this so important?

**Bank protection:** Under the *Solicitors Act 1974*, a bank cannot use money in a properly titled client account to pay off the firm's overdraft or other debts. The word "client" acts as a red flag to the bank, telling them "This money is not ours to touch."

**Clarity:** It prevents any accidental confusion between office and client funds within the firm.

### 3.3 Authorised Banks and the Designated Deposit Account

The client account must be held at a bank or building society authorised by the SRA in England and Wales. The SRA keeps a list of these. You can't use just any bank.

Sometimes, you will hold a large sum of client money for a long time (e.g., damages for a child, held until they turn 18). In these cases, it's fair to the client to earn interest on their money. To do this properly, you can open a separate designated deposit client account.

This is a specific client deposit account for one client's money. The client gets all the interest earned (after tax). It shows the client you are actively managing their money for their benefit.

For smaller amounts or shorter periods, money is held in the general client account. The firm must then pay the client a fair sum of interest, based on its own policy.

### 3.4 The Prohibition on Using a Client Account as a Banking Facility

This is one of the most important rules. A client account is not a bank. You cannot use it to provide general banking services to clients or third parties.

*Rule 3.3* is clear: "You must not use a client account to provide banking facilities to clients or third parties. Payments into, and transfers or withdrawals from, a client account must relate to the provision of regulated services."

#### 3.4.1 Case Law and SRA Guidance on "Banking Facilities"

Providing a "banking facility" means using the client account for payments that have no real connection to the legal work you are doing.

#### Example of a BREACH

A client wins a large personal injury settlement. The money is in your client account. The client then asks you to:

- Pay their monthly credit card bill from the account.
- Transfer money to their cousin overseas.

- Write a cheque for their child's school fees.

Why is this wrong? The legal work (the personal injury claim) is finished. These payments are for the client's general living expenses. The client should receive the funds into their own bank account and manage these payments themselves. Your convenience is not a valid reason.

### **3.4.2 Distinguishing Legitimate Legal Activity from Improper Banking**

So, what is allowed? Payments that are an integral part of the legal transaction.

#### **Example of a PERMITTED payment**

Acting in a house sale, you pay the estate agent's fees, the stamp duty, and the estate agent's commission from the sale proceeds in the client account.

Why is this okay? These payments are directly related to the legal transaction you are handling. You are not just moving money for the client's convenience.

The key question to ask is whether there is a proper, legally connected reason for the money to pass through the client account rather than the client handling it directly from their own bank account. If the answer is "no," you are likely providing a banking facility.

### **3.4.3 "Rolled-Up" Costs and Money Laundering Red Flags**

A major red flag for the SRA and for money laundering is the practice of "rolling-up" costs.

#### **Scenario**

A client constantly instructs you on property deals that mysteriously never complete. They send you large sums for "deposits and costs." You pay the money in and out of the client account, deducting your fees each time, and returning the balance.

Why is this suspicious? There is no genuine legal transaction. Your client account is being used to make the client's funds look "clean" by passing them through a reputable law firm. This is a classic money laundering technique.

A breach of *Rule 3.3* is serious even if no money laundering is proven. It shows a failure to protect the profession's integrity.

### **3.5 Permitted Withdrawals: An Exhaustive List**

A solicitor can only take money out of a client account for a very limited set of reasons. This list is strictly limited and allows no flexibility..

#### **3.5.1 For the Client's Purpose (Proper Instructions)**

Money can only be withdrawn from the client account to complete the legal transaction it was intended for, such as sending completion funds or paying a barrister's fee as instructed. Each payment must relate directly to the client's matter and be properly authorised to ensure the solicitor acts within their fiduciary duty.

#### **3.5.2 Transfer to Office Account for Costs (Strict Process)**

Funds may be transferred from the client account to the office account only after a bill or written cost notice (or other written notification) has been delivered and if there is enough money in the client account for that specific client to cover the transfer. This ensures transparency and prevents unauthorised or premature use of client funds.

#### **3.5.3 Return to Client**

When a legal matter concludes or when a client requests the return of their funds, the solicitor must repay the balance held in the client account without undue delay. Prompt repayment demonstrates transparency and ensures compliance with the *SRA Accounts Rules*, which require solicitors to hold client money only for as long as there is a valid reason to do so. Retaining funds without valid reason can constitute a regulatory breach and may undermine client trust.

#### **3.5.4 Payment of a Disbursement**

Solicitors are permitted to withdraw money from the client account to pay disbursements directly related to the client's case, such as court fees, search fees, expert's report or counsel's

charges. These payments must clearly connect to the legal services being provided and be properly authorised or supported by client instructions. Accurate recording of such disbursements ensures both compliance and a transparent audit trail of how client funds are used.

### **3.5.5 Bank Charges and Interest Properly Due**

Withdrawals may also be made from the client account to pay legitimate bank charges arising from that account or to remit interest owed to clients. Such transactions must be limited to charges directly attributable to the client account itself and must be supported by accurate records. Where interest is payable, firms must follow their written interest policy to ensure that clients receive a fair and transparent amount consistent with the *SRA Accounts Rules 2019*.

## **3.6 The Withdrawal Process: Proper Authority, Signatures, and Audit Trail**

Taking money out of a client account is a big deal. It must be properly controlled.

**Dual authority:** Most firms require two signatures on a client account cheque, or dual authorisation for an electronic transfer. One person should prepare the payment, and a different, more senior person should authorise it.

**Audit trail:** For every withdrawal, there must be a clear, documented reason that links back to one of the permitted reasons. This is usually recorded in the client ledger and supported by a bill or client instruction on the file.

**Supervision:** The Rules require all withdrawals to be "appropriately authorised and supervised."

## **3.7 Accounting Entries for Withdrawals from a Client Account**

Let's use our double-entry knowledge. When money leaves the client account, two things happen:

1. The Client Bank Account (an Asset) decreases.
2. Your obligation to the client (a Liability) decreases.
  - To decrease an Asset, you CREDIT.
  - To decrease a Liability, you DEBIT.

The double entry for ANY withdrawal from the client account is always:

- DEBIT [Client Name] Ledger Account
- CREDIT Client Bank Account

**Illustration:** You pay a barrister's fee of £1,500 for Client Maria from the client account.

Client Bank Account			
Date	Details	Debit (Dr)	Credit (Cr)
05/11	Maria - on account	5,000	
10/11	Barrister - for Maria		1,500

Client: Maria Matter: Litigation	Business	Client		
Date	Details	Debit (Dr)	Credit (Cr)	Balance
05/11	Client Bank		5,000	5,000 Cr
10/11	Barrister Fee	1,500		3,500 Cr

This shows the firm has reduced its obligation to Maria by £1,500 because it has spent that money on her behalf, as instructed.

### 3.8 Client Account Cheques, Bank Transfers, and Electronic Payments

The method of payment must be secure and create a clear audit trail.

**Cheques:** When payments are made by cheque, they must be clearly identified as being drawn from the client account to avoid confusion with office funds. Each cheque should be sequentially numbered, securely stored, and signed in accordance with the firm's authorisation procedures, ideally by two authorised signatories.

**Bank transfers (BACS/CHAPS/faster payments):** Electronic transfers are the most common and efficient payment method in modern practice. The firm's online banking system must be protected by robust security measures, such as two-factor authentication, to prevent unauthorised access. Each transfer must include a clear payment reference identifying the client and matter so that both the firm and the recipient can easily trace and verify the transaction.

**Audit trail:** Every payment from the client account, regardless of method, must be fully recorded in the client ledger. This record must show the date, amount, payee, and reason for the payment, and it must correspond exactly with entries on the bank statement. Maintaining an accurate audit trail ensures transparency, supports regulatory compliance, and enables effective internal and external auditing.

### 3.9 Conclusion

The client account embodies the solicitor's duty of trust and integrity, forming the cornerstone of financial propriety within legal practice. Its statutory trust status and the rules surrounding its operation are designed to prevent misuse, mixing of funds, and the inadvertent exposure of client money to risk. By strictly limiting the purposes for which money may be held or withdrawn, the *SRA Accounts Rules* reinforce both fiduciary accountability and public confidence in the profession's financial conduct.

Ultimately, the management of client accounts demands precision, discipline, and ethical awareness. Each payment, transfer, or withdrawal must serve a legitimate, transaction-

related purpose and be clearly supported by documentation. The solicitor's adherence to these principles ensures that the client account remains not only a legal safeguard but also a symbol of the profession's reliability, transparency, and moral responsibility in handling client assets.



# 4

## SEPARATION OF FUNDS AND ACCOUNTING RECORDS

The management of client and office money lies at the heart of the solicitor's financial responsibilities, with the *SRA Accounts Rules 2019* establishing the fundamental principle of absolute segregation between the two. Client money, held on statutory trust, belongs beneficially to the client and must be kept in a separate client account, while office money represents the firm's own funds. Maintaining this strict division safeguards client assets, prevents misuse, and ensures the integrity of financial reporting. A breach of segregation undermines the trust that forms the foundation of the solicitor–client relationship and may constitute serious professional misconduct.

This chapter examines how solicitors must operate both client and office accounts in compliance with regulatory and ethical standards. It explores the purpose of the office account, the operation of client ledgers and cash books, and the essential control mechanism of bank reconciliation. It also addresses the correct treatment of mixed receipts and the procedures that ensure every transaction is accurately recorded, authorised, and traceable. Together, these systems form the backbone of financial governance within legal practice, ensuring transparency, accountability, and the protection of client money.

## **4.1 The Core Principle: Absolute Segregation of Client and Office Money**

Imagine you're organising a party. You have one bowl for the sweets you're selling to raise money for the school trip (Client Money), and another bowl for your own sweets that you bought with your pocket money (Office Money). You would never, ever mix them up, because the school trip money isn't yours to eat!

This is the core principle of solicitors' accounts; Absolute Segregation.

Client Money belongs to the client. It must be kept in a client bank account.

Office Money (or Business Money) belongs to the firm. It must be kept in an office bank account.

Mixing them is one of the most serious breaches of the *SRA Accounts Rules*. It destroys the "statutory trust" that protects client money and makes it impossible to know who owns what. Your entire accounting system is built to enforce this separation.

## **4.2 The Office Account: Purpose and Use for Firm Money**

The office account is the firm's own current account. It's used for all the firm's business transactions, just like any other company.

Money that goes INTO the office account:

- Payments from clients for bills you have already sent.
- Money to reimburse the firm for a disbursement it has already paid.
- The firm's profits, used to pay salaries, rent, electricity, and other business expenses.

A client's disbursement must not be paid from the office account unless sufficient client funds have first been transferred to cover the expense, or the firm has chosen to advance the payment as a temporary loan, which then becomes client money until reimbursed.

### 4.3 Client Ledgers: The Indispensable Record for Each Client Matter

The client bank account is a single pool of money for all clients. How do you know how much of that pool belongs to Client A versus Client B? The answer is the Client Ledger.

A Client Ledger is a separate record (now almost always a screen in your software) for each individual client and matter. It's like a mini bank statement for that specific client.

#### 4.3.1 The Three-Tier System: Client Ledger, Client Cash Book, Bank Reconciliation

A well-controlled system has three key parts that act as checks and balances on each other.

1. **Client ledgers:** These are individual records showing all financial transactions for each client and matter, detailing money received, payments made, and the running balance. The total of all client ledger balances must always equal the amount held collectively in the client account.
2. **Client cash book:** This is a chronological record of every transaction in the client bank account, showing all receipts and payments regardless of client. The final balance in the cash book must match the combined total of all client ledgers to ensure accuracy.
3. **Bank reconciliation:** This is the process of comparing the firm's internal records with the actual balance shown on the bank statement. Any difference between the two must be identified and corrected promptly to maintain accurate and transparent financial records.

If the three balances do not match, it signals an accounting error or discrepancy that must be identified and corrected immediately to protect client funds.

#### 4.3.2 Contents of a Client Ledger: Mandatory Entries and Descriptions

Every entry on a client ledger must be clear. The *SRA Rules* require it to contain:

1. The date of the transaction.

2. A sufficient description (e.g., "Funds received on account," "Payment to HM Land Registry for search," "Transfer to office account re bill dated 01/11/2024").
3. The amount of the receipt or payment.
4. The running balance for that client.

### Example

Client: David Lee  Matter: Purchase of 1 High Street				
Date	Details	Money IN (Cr)	Money OUT (Dr)	Balance
01 Oct	Received on account of costs	5,000		5,000 Cr
05 Oct	Paid Local Search		150	4,850 Cr
10 Oct	Paid Land Registry fee		270	4,580 Cr
15 Oct	Transfer to office account (Bill ref: INV123)		1,200	3,380 Cr

This ledger shows that the firm is currently holding £3,380 for David Lee.

## 4.4 Dealing with Mixed Receipts: The Process in Detail

A mixed receipt is a single payment from a client that contains both Client Money and Office Money. This happens very often.

#### 4.4.1 Identifying a Mixed Receipt

**Scenario:** You send a client a completion statement for a property purchase. It shows they need to send £200,000 for the purchase (Client Money) and £1,500 for your billed fees (Office Money). They send you one cheque for £201,500.

This is a mixed receipt. You have to separate it.

#### 4.4.2 The Accounting Procedure for Apportionment

You have two choices, but you must act PROMPTLY.

##### **Option A; Split the Cheque (Ideal but often impractical)**

You pay £200,000 into the client account and £1,500 into the office account. Most banks no longer offer this service.

##### **Option B (The Common Method)**

Pay the whole amount into one account and transfer. You can pay the entire £201,500 into the client account and then promptly transfer the £1,500 office money to the office account.

**The Double Entry would be:**

##### **1. Receive the full amount into client account:**

- DR Client Bank Account £201,500
- CR Client Ledger £201,500

##### **2. Transfer the office money out:**

- DR Client Ledger £1,500
- CR Client Bank Account £1,500
- DR Office Bank Account £1,500
- CR Client Ledger (Business Column) £1,500

### 4.4.3 Paying the Office Element into the Client Account

It is also permissible to pay the whole mixed receipt into the office account and then transfer the client money to the client account. However, this is riskier because client money is temporarily in the office account. The transfer of the client money must be done even more promptly.

### 4.5 The Client Cash Book: Recording All Movements Chronologically

The Client Cash Book is the diary of the client bank account. It lists every single transaction, every receipt, every payment in date order. It doesn't care which client it's for; it just records the total movement of the whole client account.

Client CashBook				
Date	Details	Debit (Dr)	Credit (Cr)	Balance
01 Oct	Client A - on account	10,000		10,000 Dr
02 Oct	Client B - on account	5,000		15,000 Dr
03 Oct	Paid Search for Client A		200	14,800 Dr
04 Oct	Client C - on account	8,000		22,800 Dr

The total of all the individual client ledger balances (Client A + Client B + Client C) must always equal the final balance in this cash book.

### 4.6 The Bank Reconciliation Process: A Key Control

This is one of the most important controls a firm has. It is the process of checking that your internal records (the Client Cash Book) match the external reality (the Bank Statement).

#### **4.6.1 Purpose and Frequency of Reconciliation**

The purpose of bank reconciliation is to find and correct any differences between your records and the bank's. This is often the first place fraud or errors are discovered.

The *SRA Rules* require to get a bank statement at least every five weeks and to perform a reconciliation at least that often.

### **4.7 Conclusion**

The separation and proper management of client and office money are essential to maintaining both legal compliance and professional credibility. Through rigorous controls such as client ledgers, the client cash book, and regular bank reconciliations, solicitors can demonstrate that every transaction is accounted for and that client funds are safeguarded at all times. Adherence to these principles is not merely an administrative exercise but a reflection of the solicitor's ethical duty of care and fiduciary responsibility.

Ultimately, financial accuracy and transparency uphold the reputation of the legal profession and reinforce public trust in solicitors as custodians of client funds. The *SRA Accounts Rules* ensure that every firm, regardless of size or structure, operates under a consistent standard of accountability. By applying these rules diligently and maintaining absolute segregation of funds, solicitors fulfil their statutory obligations and exemplify the integrity upon which the profession depends

# 5

## INTEREST ON CLIENT MONEY

The payment of interest on client money reflects one of the solicitor's most fundamental fiduciary duties; ensuring that clients are not financially disadvantaged while their funds are held in trust. *Rule 7.1* of the *SRA Accounts Rules* requires solicitors to account to clients for a fair sum of interest on any money held on their behalf, reinforcing the profession's ethical and regulatory commitment to fairness and transparency. Unlike rigid financial regulations, this duty operates on the principle of reasonableness: firms must develop and apply policies that balance administrative practicality with the client's entitlement to a just return. In essence, the obligation to pay a fair sum of interest safeguards both client confidence and the integrity of the profession.

The determination of what is "fair" requires professional judgment, guided by prevailing interest rates, the amount and duration of funds held, and the accessibility of comparable accounts. Firms must also distinguish between genuine obligations and minor, negligible sums under the *de minimis* rule, ensuring that their policies are both proportionate and consistently applied. Whether client money is held in a pooled account or a designated deposit account, the principle remains constant, the client's money must work for the client's benefit.

### **5.1 The Ethical and Regulatory Duty to Pay a Fair Sum of Interest**

Imagine you are looking after your neighbour's £100 while they are on holiday. If you put that money in a savings account, it would earn interest. When they return, it would be wrong to keep that interest for yourself. The interest belongs to them because it was earned on their money.



This is the core principle for solicitors. When you hold client money, you have a duty to act in their best interests (*SRA Principle 7*). This includes ensuring they do not lose out on the interest their money could have earned.

The *SRA Accounts Rules (Rule 7.1)* make this duty explicit: You must account to clients or third parties for a fair sum of interest on any client money held by you on their behalf.

This is not just about being nice; it's a regulatory requirement based on your fiduciary duty.

## 5.2 Assessing What is "Fair": The SRA Principles and Case Law

The *Rules* don't specify an exact interest rate. Instead, they use the word "fair." This means firms must use their professional judgment to create and follow a consistent policy.

A fair interest rate is one that reasonably reflects the return the client could have expected if they had held the money themselves in a similar, readily accessible account. Key factors include:

- The amount of money held.
- The length of time it is held.
- The interest rates generally available from high-street banks for instant-access deposits.

A firm's policy must be justifiable. Paying 0.1% when the average high-street bank is paying 2% would likely be considered unfair.

## 5.3 The Client's Right to Interest vs. The Firm's Discretion on *De minimis*

The client has a right to a fair sum of interest. However, the SRA recognises that calculating and paying tiny amounts of interest is administratively impractical.

This is where the *de minimis* rule applies (from the Latin maxim *de minimis non curat lex* which means "the law does not concern itself with trifles").

A firm's policy can state that it will not pay interest if the total calculated amount due to a client is below a certain threshold.

This threshold must be reasonable. For a firm dealing with private clients, a threshold of £20 or £50 might be reasonable. For a firm dealing with large commercial clients, a higher threshold would be expected.

The policy must be applied consistently to all clients.

Noteworthy is the fact that the *de minimis* rule applies to the payment, not the calculation. You should still be able to demonstrate that you have calculated the interest, even if the amount is too small to actually pay.

## **5.4 Methods of Holding Client Money for Interest Purposes**

There are two main ways to hold client money, and the interest obligation works differently for each.

### **5.4.1 The General Client Account: Pooled Money and Calculation**

This is the standard client account where money for all clients is pooled. The bank pays interest on the entire pool. The firm keeps this bulk interest. The firm then uses its policy to calculate and pay a "fair sum" to each individual client from its own office funds.

This method is administratively complex for a solicitor must calculate interest for each client but it can be financially beneficial for the firm if it earns more on the pool than it pays out.

### **5.4.2 Separate Designated Deposit Accounts: For Larger Sums or Long Periods**

For large sums (e.g., £50,000+) or money held for a long time (e.g., damages for a child), it is often fairest and simplest to open a separate designated deposit account for that specific client. The bank pays interest directly into this account. The firm then accounts to the client for all of the interest earned.

This method is transparent and ensures the client gets every penny of the return.

## 5.5 Calculating Interest on the General Client Account

A firm's interest policy should clearly state its calculation method. Common approaches will be considered below.

### 5.5.1 Agreed Rate with the Client

A firm may agree on a specific interest rate with the client in the engagement letter, giving both parties clarity and certainty. The rate should be reasonable and reflect market conditions to ensure fairness, especially for long-term or high-value matters.

### 5.5.2 Using a Reference Rate (e.g., Bank of England Base Rate)

Many firms use a benchmark like the Bank of England base rate, often slightly reduced (e.g., by 0.5–1%) to reflect administrative costs. This method ensures transparency and fairness, as it aligns with publicly available rates and standard financial practice

Example of such policy: "We will pay interest at a rate of 1% below the Bank of England base rate, subject to a minimum payment of £20."

### 5.5.3 Period of Calculation: From Clearance to Withdrawal

Interest should be calculated from the date the client's funds clear in the client account until the date you withdraw the money to pay it to the client or a third party. Most firms calculate it on a daily basis and pay it at the conclusion of the matter to ensure accuracy and fairness to the client.

## 5.6 The Process for Paying Interest to the Client

1. **Calculate:** At the end of the matter, calculate the interest due based on your firm's policy.
2. **Check *de minimis*:** If the amount is below your policy's threshold, you may not need to make a payment, but you should record the calculation.
3. **Pay:** If payment is due, it is usually made from the office account, as it is an expense of the firm fulfilling its duty. You can either:

- Send a separate cheque for the interest, or
- Add the interest to the final cheque returning the client's balance.

## 5.7 Tax Deduction and Reporting (Where Applicable)

Historically, this was complex, but the rules have simplified. Since April 2016, banks and building societies now pay interest gross (without deducting tax).

It is the client's responsibility to declare any interest received from their solicitor to HMRC, if they are liable for tax on it.

The law firm does not have to deduct tax or report it to HMRC.

## 5.8 Accounting Entries for Receiving Bank Interest

When the bank pays interest on the general client account, that interest belongs to the firm. It is the firm's reward for managing the pooled account.

The double entry is in the office accounts:

- Debit (Dr) Office Bank Account
- Credit (Cr) Interest Received Account (an Income account)

This increases the firm's assets (cash) and its income.

## 5.9 Accounting Entries for Paying Interest to the Client

When you pay interest to a client from the office account, it is an expense for the firm.

### Scenario

You pay Client Ben £30 in interest at the end of his matter.

**Option 1:** Pay interest directly from office account

Debit (Dr) Interest Payable Expense Account £30

Credit (Cr) Office Bank Account £30

**Option 2:** Transfer interest to client account first, then pay client. This is less common but sometimes used. It involves two steps:

1. Transfer from office to client account

Debit (Dr) Interest Payable Expense £30

Credit (Cr) Office Bank Account £30

Debit (Dr) Client Bank Account £30

Credit (Cr) Client Ben Ledger £30

2. Pay client from client account

Debit (Dr) Client Ben Ledger £30

Credit (Cr) Client Bank Account £30

The net effect on the client ledger is zero, but it shows a clear audit trail that the interest was handled.

## 5.10 Record-Keeping Requirements for Interest Calculations

Firms must be able to demonstrate compliance with the SRA's interest rules through proper documentation. This includes keeping a copy of the firm's written interest policy, detailed calculations showing how interest was determined for clients, clear notes on the client ledger recording any interest paid, and records of bank interest earned on the general client account. Maintaining accurate and transparent records provides evidence of fairness, consistency, and accountability in managing client money.

## 5.11 Conclusion

The duty to pay interest on client money is not merely a financial calculation but a manifestation of the solicitor's broader fiduciary responsibility. It reinforces the trust-based nature of legal practice by ensuring that clients receive the full benefit of funds held in their name. A transparent, well-documented policy on calculating and paying interest

demonstrates compliance with the *SRA's Principles* and safeguards the firm from both regulatory and reputational risks.

Ultimately, proper record-keeping, consistent application of the firm's interest policy, and timely payment of interest are vital indicators of sound financial governance. By upholding these standards, a law firm not only meets its regulatory obligations but also sustains public confidence in the legal profession's integrity, accountability, and fairness

# 6

## BREACHES OF THE SRA ACCOUNT RULES

The *Solicitors Regulation Authority (SRA) Accounts Rules* impose a strict framework to ensure that client money is handled with integrity, transparency, and accountability. Despite best efforts, breaches can occur, ranging from minor technical lapses to deliberate misconduct. Understanding the nature, causes, and corrective processes for such breaches is essential for maintaining compliance and protecting client trust. Prompt rectification and clear accountability within the firm are not just regulatory obligations but fundamental ethical duties that uphold the integrity of the legal profession.

Breaches also serve as valuable indicators of weaknesses within a firm's systems or training procedures. Identifying and analysing these errors through effective oversight, especially by the Compliance Officer for Finance and Administration (COFA), ensures lessons are learned and safeguards are strengthened. The SRA's emphasis is not only on correcting errors but also on fostering a proactive culture of compliance and transparency across all levels of practice.

### **6.1 Definition of the Word “Breach”**

A breach of the SRA Accounts Rules is any failure to follow them. Breaches exist on a spectrum, from minor, accidental errors to serious, deliberate misconduct.

## Technical Breach

This is an unintentional, one-off mistake that is quickly spotted and corrected, and where no client money is at risk. For example: A cashier pays a cheque into the client account one day later than the firm's "same-day" policy, but the money was secure in the office safe overnight.

## Substantive Breach

This is a more serious failure where client money has been, or could have been, placed at risk. These often involve a breach of the core principles. For example, using £1,000 from Client A's money to pay a bill for Client B because there wasn't enough money for Client B at that moment. This is a breach of *Rule 5.3*, even if you replace it an hour later.

## Serious Misconduct

This is a deliberate, reckless, or repeated breach, often involving dishonesty. For example, deliberately using client money to cover a shortfall in the office account, or systematically over-billing clients.

The SRA focuses on the substance and impact of a breach, not just the technicality. A pattern of small "technical" breaches can indicate a serious systemic problem.

## 6.2 The Absolute Duty to Correct Breaches Promptly on Discovery

This is a non-negotiable rule. *Rule 6.1* states: "Any breach of the *Rules* must be corrected promptly upon discovery... any money improperly withheld or withdrawn from a client account must be immediately paid into the account."

"Promptly" and "Immediately" mean taking action to rectify it without delay, the issue must be addressed at once, not postponed for later.

The duty arises as soon as anyone in the firm (a cashier, a fee-earner, the COFA) becomes aware of the breach.



### 6.3 The Role of the COFA in Overseeing the Rectification Process

The Compliance Officer for Finance and Administration (COFA) has a specific duty to ensure the firm complies with the Accounts Rules. When a breach occurs, the COFA must:

1. Ensure it is rectified immediately.
2. Investigate the root cause to prevent it from happening again.
3. Decide whether the breach is serious enough to be reported to the SRA.
4. Record the breach in the firm's breach register.

The COFA is the central point for managing the firm's response to a breach.

### 6.4 Investigating the Cause of the Breach: Root Cause Analysis

Fixing the money is the first step. Fixing the problem is the second. You must ask "Why?" until you find the underlying cause.

**Example:** An Overdrawn Client Ledger

What happened? Client X's ledger was overdrawn by £500.

Why? Because a payment of £1,500 was made for them when only £1,000 was held.

Why? Because the fee-earner authorised the payment without checking the ledger balance.

Why? Because the fee-earner didn't know how to access the ledger system.

Why? Because the firm provides no formal training on the accounts rules.

The root cause is a lack of training, not the individual's mistake. As a result, the solution is a firm-wide training, not just telling that fee-earner to be more careful.

## 6.5 Common Types of Breaches and Their Rectification

### 6.5.1 Telegraphic Transfers: Incorrect Apportionment

**Breach:** This type of breach occurs when a client sends a combined payment covering both completion funds (client money) and professional fees (office money), but the entire amount is incorrectly deposited into the firm's office account. This misallocation breaches the requirement to keep client and office money strictly segregated under the SRA Accounts Rules.

**Rectification:** The correct approach is to identify and separate the funds immediately, transferring the client's portion to the client account without delay. This ensures that client money is properly safeguarded and that the firm's accounting records accurately reflect the transaction.

### 6.5.2 Banking Cheques: Unjustified Delay

**Breach:** Leaving a client's cheque unbanked for an extended period, such as keeping it in a drawer, constitutes an unjustified delay and breaches the duty to handle client money promptly. This delay not only exposes the client's funds to unnecessary risk but also undermines trust in the firm's financial discipline.

**Rectification:** Upon discovery, the cheque must be deposited into the appropriate account immediately, and the firm should review its internal controls for receiving and processing payments. Clear Policies, such as same-day or next-day banking, can help prevent future occurrences and ensure compliance with the rule of prompt handling.

### 6.5.3 Overdrawn Client Ledger: Causes and Immediate Correction

An overdrawn client ledger is one of the most serious breaches, as it signifies that funds belonging to one client have been used for another, violating the statutory trust principle. This can occur in two ways.

**Cause 1:** By drawing a cheque against an uncleared cheque that is then dishonoured.

**Cause 2:** By simply paying out more for a client than they have in their ledger.

**Rectification:** The rectification must be immediate; any shortfall in the client account must be replaced from the firm's own funds. Beyond rectification, the firm should investigate how the error occurred and strengthen controls to prevent recurrence.

#### 6.5.4 Withdrawal without Authority

**Breach:** This arises when a firm transfers money from the client account to the office account before issuing a bill or obtaining proper authorisation from the client. Doing so effectively uses client money for the firm's benefit without consent, breaching both fiduciary and regulatory duties.

**Rectification:** The immediate corrective action is to return the funds to the client account and only make the transfer again once a valid bill has been delivered. Firms should ensure that withdrawals are properly authorised, supported by documentation, and reviewed by a responsible officer.

### 6.6 Accounting Entries to Correct an Overdrawn Client Ledger

When a client ledger is overdrawn, you have used other clients' money. To correct this, you must inject the firm's own money into the client account.

#### Scenario

Client Y's ledger has a balance of £1,000 Credit (Cr). You pay a £1,500 search fee for them, making their ledger £500 DR. This is a breach.

Step 1: Transfer office money to the client account to cover the shortfall.

- Debit (Dr) Client Y Ledger Account £500 (This brings his ledger balance back to zero)
- Credit (Cr) Client Bank Account £500
- Debit (Dr) Office Bank Account £500
- Credit (Cr) Client Y Ledger Account (Business Column) £500

Client: Y Matter:	Business	Client		
Date	Details	Dr	Cr	Balance
...	Balance			1,000 Cr
...	Paid Search		1,500	500 Dr
...	Office Money Injection	500		0

The client ledger is now correct. The firm has effectively lent £500 to Client Y, who now owes this to the firm (shown in the business column).

## 6.7 Accounting Entries to Reimburse the Client Account (from Office Money)

This is the same concept as above. Any time the client account is short, you must reimburse it from the office account.

General Double Entry to Reimburse Client Account:

- Debit (Dr) Office Bank Account
- Credit (Cr) Client Bank Account

This is accompanied by the ledger entries to show which client caused the shortfall and now owes the money to the firm.

## 6.8 Reporting Breaches to the SRA: When is it Mandatory?

The COFA has a duty to report serious breaches to the SRA. A breach is likely to be "serious" if:

1. It poses a risk to client money (e.g., an overdrawn ledger).
2. It arises from dishonesty or theft.
3. It is a systemic or recurring problem that the firm has failed to address.
4. It is significant in scale or impact.

When in doubt, the COFA should err on the side of reporting. Failure to report a serious breach is itself a disciplinary matter for the COFA and the firm.

## 6.9 The Importance of a Breach Register and Internal Reporting

Every firm must maintain a Breach Register. This is a log of every breach, no matter how small.

A good breach register should record:

1. Date the breach was discovered.
2. Description of the breach.
3. The amount of money involved.
4. How and when it was rectified.
5. The root cause.
6. Action taken to prevent recurrence (e.g., "Staff training delivered").
7. Whether it was reported to the SRA.

### Importance of the Breach Register

1. **Demonstrates compliance:** It shows the SRA that the firm takes breaches seriously and manages them properly.
2. **Identifies trends:** A register can reveal if the same type of breach keeps happening, pointing to a major systemic flaw.

3. **Promotes a culture of honesty:** Encouraging staff to report minor breaches without fear makes it more likely that major issues will be caught early.

## 6.10 Conclusion

Managing breaches of the *SRA Accounts Rules* is about more than simply fixing numerical errors; it is about maintaining the profession's reputation for trust and financial probity. Firms are expected to correct breaches immediately, record them accurately, and take steps to prevent recurrence through systemic improvement and staff education. The COFA plays a central role in ensuring both swift rectification and appropriate reporting to the SRA where necessary.

Ultimately, an effective breach management process reflects a firm's commitment to ethical conduct and regulatory diligence. Maintaining a breach register, investigating root causes, and fostering open reporting channels demonstrate that the firm not only understands its obligations but also values the trust placed in it by clients and the wider public

# 7

## CLIENT LEDGERS, BILLS, AND RECONCILIATION

Managing client ledgers, disbursements, reconciliations, and VAT obligations lies at the heart of sound legal accounting practice. This section explores how firms must maintain precision and transparency in handling client and office money to uphold professional and regulatory standards. It outlines the methods, controls, and accounting principles that ensure client funds remain safeguarded and accurately recorded at every stage of a transaction.

By linking theory with practical procedures, it explains how correct billing, reconciliation, and VAT treatment prevent compliance risks and strengthen client trust. Together, these practices form the framework for ethical financial management and demonstrate a solicitor's duty of integrity, accountability, and professionalism.

### **7.1 The Client Ledger as the Central Record: Structure and Best Practice**

The Client Ledger is the heartbeat of solicitors' accounting. It is a dedicated record for each client matter, tracking every penny you hold for them and every penny they owe you. Think of it as a dedicated bank statement and invoice tracker combined, for that single client.

A well-structured ledger is split into two main columns:

1. Client Money Column which tracks all money held in the client account for the client.

2. **Business Money Column** which tracks all money the client owes to the firm (for fees and disbursements).

### Best Practice for Client Ledgers

1. **Clear descriptions:** Every entry must have a clear narrative (e.g., "Funds on account," "Payment to HMLR for search," "Transfer to office re Q3 bill").
2. **Running balance:** The balance must be updated after every single transaction.
3. **Timeliness:** Entries should be made on the day of the transaction.
4. **Accuracy:** The ledger must be a precise and reliable record.

## 7.2 The Reconciliation Trinity: Reconciling Ledgers, Cash Book, and Bank Statement

This is the essential control process that proves your records are accurate. It involves checking that three different records all tell the same story.

1. **List of client ledger balances:** The total of all individual client ledger balances (what you think you hold for all clients).
2. **Client cash book balance:** The balance of the client bank account according to your firm's internal records.
3. **Bank statement balance:** The balance of the client bank account according to the bank.

The rule is that the total of #1 **MUST** equal #2, which must equal #3 after accounting for timing differences (like unpresented cheques). If they don't match, you must investigate and correct the error immediately. This reconciliation must be performed at least every five weeks.

## 7.3 Disbursements: Definition and Treatment - The Deep Dive

A disbursement is a payment you make to a third party (like a barrister, a search company, or a court) on behalf of your client. The core question is: "Whose purchase is this, really?"



The answer determines everything: which bank account you use, how you treat VAT, and what you put on the client's bill. Getting this wrong means getting your VAT wrong, which is a serious compliance issue.

To understand it, we use two methods: the Principal Method and the Agency Method. Let's break them down with a simple analogy.

### **The Restaurant Analogy**

Imagine you and a friend are at a restaurant.

**Scenario A** (Principal Method): You order food for the table. The waiter brings one bill *to you* for everything—the food and the service. You pay the whole bill with your card, and your friend gives you cash for their share. You are the "principal."

**Scenario B** (Agency Method): Your friend is running late. They call you, tell you their exact order, and ask you to give their credit card to the waiter. The waiter brings two separate bills: one for your food and service (to you), and one just for your friend's food (to your friend). You hand your friend's card to the waiter for their bill. You are the "agent."

Now, let's apply this to a law firm.

#### **7.3.1 The Principal Method: You Are the Buyer (VAT on Bill)**

This method is used when the supplier's invoice is made out **TO YOUR LAW FIRM**. In this instance, the supplier has sold the service to you. You have then used that service to help your client. Therefore, you are re-selling that service to your client as part of your overall legal service.

Because you are re-selling it, you **MUST ADD VAT** on top of the cost when you include it on your client's bill. The VAT must be paid for from your **OFFICE ACCOUNT**. It was your purchase.

#### **Example: Paying a Surveyor (Invoice to the Firm)**

You instruct a surveyor for a client's property dispute. The surveyor's invoice for £1,000 + £200 VAT is addressed to "Smith & Co Solicitors."

1. You Pay the Surveyor from your OFFICE account:
  - You pay £1,200.
  - You can reclaim the £200 VAT from HMRC.
2. You Bill the Client: On your bill, you show:
  - Professional Charges: [Your Fees]
  - Surveyor's Fee: £1,000
  - VAT: £200 (on your fees) + £200 (on the surveyor's fee) = £400
  - Total: Your Fees + £1,400

The client ends up paying VAT on the surveyor's fee. If the client is VAT-registered, they can reclaim it. If they are a private individual, this costs them more.

### **7.3.2 The Agency Method: The Client Is the Buyer (VAT on Disbursement)**

This method is employed when the supplier's invoice is made out TO YOUR CLIENT.

The supplier has sold the service directly to your client. You are just the postbox or the paying agent. You are not re-selling the service.

As a result, there is no need for VAT cost to be added to the cost. You simply pass on the exact cost to the client. The VAT treatment is between the original supplier and your client. VAT can be paid from the CLIENT ACCOUNT, if you hold enough of their money, as you are simply moving their money on their behalf.

#### **Example: Paying a Court Fee (Invoice to the Client)**

You pay a court fee of £500 for your client's application. The court fee is a statutory fee payable by the client. The "invoice" (the court form) is in the client's name.

1. You Pay the Court from the CLIENT account:
  - You pay £500. There is no VAT on court fees.
2. You Bill the Client: On your bill, you show:

- Professional Charges: [Your Fees] + VAT
- Disbursements: Court Fee: £500 (No VAT added)
- Total: Your Fees (inc. VAT) + £500

The client pays the net cost of the disbursement. There is no extra VAT.

### 7.3.3 Criteria for a True Disbursement (Agency Method)

You can't just call anything a disbursement to avoid charging VAT. HMRC has strict rules. All of the following must be true:

1. **You acted as the client's agent:** The client knew you were just handling the payment for them.
2. **The client received the goods or services:** The third party supplied them directly to the client. (This is why your train ticket to see a client is *not* a disbursement—you received the transport service, not the client).
3. **The client was legally liable to pay the third party:** The client, not you, is ultimately on the hook for the bill.
4. The client authorised you to make the payment.
5. **The service is separate from your supply:** It is not an integral part of your legal advice. (e.g., You use a search result to advise a client - the search is part of your service. A doctor's report sent directly to the client for their own information is a disbursement).

Common TRUE Disbursements (Agency Method) include: court fees, Stamp Duty Land Tax (SDLT), Land Registry registration fees, probate fees, and medical reports ordered for the client's own purposes.

### 7.3.4 Recharges (e.g., Photocopying, Travel): Treatment as Profit Costs

Most other expenses you incur are NOT disbursements. They are costs of running your business and providing your service. These are called "recharges" or "incidental expenses."

You purchased these items for yourself to enable you to do your job. You **MUST ADD VAT** when you recharge them to the client. They are treated exactly like your professional fees.

The SRA states that it is not normally appropriate to make a separate charge for items like normal postage, phone calls, or routine photocopying. You should include these costs within your professional fee. However, for unusual, high-cost items (e.g., colour photocopying a large trial bundle), you can recharge them.

#### Examples of RECHARGES (Principal Method):

- Travel expenses: Train tickets, taxi fares, mileage. *You* travelled, not the client.
- Postage and courier fees: You are sending your work product.
- Photocopying and printing.
- Telephone calls.
- Online search fees (e.g., company search, Land Registry search). *You* are using the information to provide advice.

#### Summary Table

Feature	Principal Method (Recharge)	Agency Method (True Disbursement)
Invoice Addressed To	The Law Firm	The Client
What's Really Happening?	Firm buys and re-sells	Firm is a paying agent
VAT on Client's Bill?	YES, you add VAT	NO, you pass it on as-is
Paid From Which Account?	Office Account	Client Account (if funds available)
Example	Online search fee	Court Fee

## **7.4 Submitting a Bill of Costs to the Client**

### **7.4.1 Content and Form of a Bill**

A bill must be clear and contain:

1. Your firm's name and address.
2. The client's name and address.
3. A unique bill number and date.
4. A clear description of the legal services provided.
5. A breakdown of professional charges, disbursements, and VAT.
6. The total amount due.

### **7.4.2 Informing the Client of their Rights**

The bill should state the client's right to challenge the bill through assessment by the court and how to make a complaint.

### **7.4.3 Accounting Entry on Submission of a Bill**

When you issue a bill, no cash moves, but you now have a right to be paid. The client's debt to you increases.

#### **Double Entry:**

- Debit (Dr) Client Ledger (Business Column) [Total of Bill inc. VAT]
- Credit (Cr) Profit Costs Account [Professional Fees]
- Credit (Cr) HMRC VAT Account [VAT on fees and recharges]

This shows the client now owes the firm money.

## **7.5 Reduction and Abatement of Bills: Client Challenges and Agreements**

If a client successfully challenges a bill and you agree to reduce it, you must also reduce the VAT.

### **7.5.1 Accounting Entry for Reducing a Bill**

You reverse part of the original billing entry.

- Debit (Dr) Profit Costs Account [Reduction in Fees]
- Debit (Dr) HMRC VAT Account [Reduction in VAT]
- Credit (Cr) Client Ledger (Business Column) [Total Reduction]

You must also issue a VAT credit note to the client.

## **7.6 Payment of Bills: Transferring Money from Client to Office Account**

### **7.6.1 The Process and Timing**

Once a bill has been delivered, you can transfer money held for the client in the client account to the office account to pay it. This must be done promptly.

### **7.6.2 Accounting Entry for Paying a Bill**

#### **Double Entry:**

- Debit (Dr) Client Ledger (Client Column) [Amount of transfer]
- Credit (Cr) Client Bank Account [Amount of transfer]
- Debit (Dr) Office Bank Account [Amount of transfer]
- Credit (Cr) Client Ledger (Business Column) [Amount of transfer]

This reduces the money you hold for the client and reduces the debt they owe you.

## 7.7 VAT in Legal Practice - The Deep Dive

Value Added Tax (VAT) is a transaction tax. For a law firm, you are a "taxable person" – you must charge VAT on your services and pay it over to the government, but you can also reclaim VAT you pay on business purchases.

Think of yourself as a tax collector for HMRC. You don't keep the VAT; you're just the middleman who collects it from clients and sends it to the government.

### 7.7.1 VAT on Professional Charges (Profit Costs)

This is the straightforward part. When you do legal work, you are making a "taxable supply." You must charge VAT on top of your fees.

- Your Fee: £1,000
- VAT @ 20%: £200
- Client Pays: £1,200

You now have £200 that belongs to HMRC. You are holding it for them until it's time to pay it over.

### 7.7.2 VAT Treatment of Disbursements vs. Recharges - The Critical Difference

This builds directly on the methods of disbursements. The VAT treatment is the key difference between the two methods.

#### **The "Recharge" (Principal Method) - YOU ARE THE BUYER**

You bought something (like a search) to help you do your job. You used it to provide advice. You are now re-selling that cost to the client as part of your service.

Because it's part of your service, you **MUST ADD VAT** on top of the cost.

For example: You buy a Land Registry search for £10. You use it for your advice. On the bill, you charge:

- Search Fee: £10

- VAT on Search: £2
- Client pays £12 for the search.

### **The "True Disbursement" (Agency Method) - THE CLIENT IS THE BUYER**

You are just the postman. The client bought the thing (like a court fee), and you are simply handling the payment for them. It is not part of your service.

Because it's the client's purchase, you DO NOT ADD VAT. You just pass on the exact cost.

For example: You pay a court fee of £100 for the client. The court's "invoice" is to the client. On the bill, you charge:

- Court Fee: £100
- Client pays £100 for the fee. No VAT.

### **Importance**

1. **For the client:** If they are a private individual, they save money if it's a true disbursement (no extra VAT).
2. **For a VAT-registered client:** They can reclaim the VAT from HMRC either way, but the paperwork is different.
3. **For you (the firm):** Getting it wrong means you undercharge or overcharge VAT, leading to fines from HMRC.

### **7.7.3 Accounting Entries for VAT Payable and Reclaimable**

Let's track the VAT money. We use a special ledger account called the "HMRC VAT Account." This account tracks how much VAT you owe to the government versus how much the government owes you.

#### **Rule of Thumb for the HMRC VAT Account**

- CREDIT the account when you charge VAT to a client (you now owe this money to HMRC).



- DEBIT the account when you pay VAT to a supplier (HMRC now owes this money back to you).

### **Scenario 1**

You bill a client for £1,000 fees + £200 VAT.

What's happening: You have collected £200 for HMRC. Your debt to HMRC has increased.

Double Entry:

- Debit (Dr) Client Ledger (Business) £1,200 (Client now owes you £1,200)
- Credit (Cr) Profit Costs £1,000 (You earned £1,000 in fees)
- Credit (Cr) HMRC VAT Account £200 (You now owe HMRC £200)

### **Scenario 2**

You buy a new office printer for £500 + £100 VAT.

What's happening: You have paid £100 VAT to a supplier. HMRC now owes you this back.

Double Entry:

- Debit (Dr) Office Equipment £500 (You gained an asset)
- Debit (Dr) HMRC VAT Account £100 (HMRC now owes you £100)
- Credit (Cr) Office Bank Account £600 (You paid £600 cash)

### **The Quarterly Reckoning**

At the end of the quarter, your HMRC VAT Account might look like this:

- Total VAT Charged to Clients (CREDITS): £10,000
- Total VAT Paid to Suppliers (DEBITS): £2,000
- Net Amount Owed to HMRC: £8,000

You then pay HMRC £8,000 and reset the account.

## 7.8 Transfers of Money - The Deep Dive

A transfer is moving money from one "pot" to another. In legal accounting, there are two fundamental types of transfers, and confusing them is a common error.

### 7.8.1 Cash Transfers: Moving Physical Money Between Bank Accounts

This is what you normally think of as a transfer. Physical money moves from one bank account to another.

#### Classic Example

Transferring money from the Client Account to the Office Account to pay your bill.

What's Happening: The client's money is physically leaving the protected "client" bank account and entering the firm's "office" bank account. The money changes its nature from client money to office money.

This occurs only after you have sent a bill to the client.

#### Double Entry for a Cash Transfer (e.g., transferring £800 for fees)

Because money moves between bank accounts, you must record both the payment from one and the receipt into the other.

##### 1. Payment from Client Account:

- Debit (Dr) Client Ledger (Client Column) £800 (We are reducing the amount we hold for the client)
- Credit (Cr) Client Bank Account £800 (Money physically leaves the client account)

##### 2. Receipt into Office Account:

- Debit (Dr) Office Bank Account £800 (Money physically arrives in the office account)
- Credit (Cr) Client Ledger (Business Column) £800 (We are reducing the debt the client owes us for the bill)

## **7.9 Dealing with Third-Party Cheques, Dishonoured Cheques, and Write-Offs**

### **Third-Party Cheques**

A cheque made payable to the client, not the firm. You cannot pay this into your client account. You must forward it to the client and record its receipt and dispatch on the file.

### **Dishonoured Cheques**

A client cheque you paid in "bounces." You must reverse the original receipt entry. If you have already spent that money, it will have caused an overdrawn client ledger, which you must rectify immediately with office money.

### **Write-Offs**

If a client debt is irrecoverable (a bad debt), you write it off.

Double Entry:

Debit (Dr) Bad Debts Expense Account

Credit (Cr) Client Ledger (Business Column)

You may be able to reclaim the VAT from HMRC after six months.

## **7.10 Conclusion**

Maintaining integrity in solicitors' accounts requires more than technical precision; it demands a proactive commitment to ethical and regulatory diligence. This chapter demonstrates that clear client ledgers, consistent reconciliation, and accurate VAT treatment are not merely administrative tasks but safeguards of trust. By adhering to best practices in record-keeping, billing, and fund transfers, firms demonstrate accountability to both clients and the SRA.

Ultimately, the careful management of client and office money reflects the profession's wider responsibility to act with honesty, competence, and transparency. A solicitor who maintains

well-structured records, investigates discrepancies, and applies sound accounting principles not only ensures compliance but also strengthens the reputation of the legal profession as a whole

# 8

## SPECIFIC ACCOUNT ARRANGEMENTS

This chapter explores the alternative mechanisms through which solicitors may handle, manage, or supervise client-related funds outside the traditional client account structure. It examines joint accounts, client-operated accounts, and third-party managed accounts (TPMAs), outlining their regulatory foundations, operational safeguards, and record-keeping obligations. Each arrangement carries distinct responsibilities, requiring solicitors to maintain transparency, protect client interests, and ensure compliance with both SRA and FCA frameworks.

By analysing their application in contexts such as trusts, estates, and property transactions, the chapter demonstrates how these models balance client protection with practical efficiency. It highlights the shift from direct handling of money to supervisory control, emphasising fiduciary duties, informed client consent, and robust audit trails as the cornerstone of ethical financial management in legal practice.

### **8.1 Operation of a Joint Account**

#### **8.1.1 Definition and Purpose (e.g., Joint Ventures, Co-trustees)**

A joint account is a bank account held in the names of both the law firm (or a solicitor within it) and another party, typically a client or co-trustee. Both (or all) named account holders can independently operate the account, unless specific signing restrictions are put in place.

## Common Examples

- **Probate/Estates:** A solicitor who is a named executor in a will opens an account with the other lay executor(s).
- **Trusts:** Where solicitors are co-trustees with others.
- **Joint Ventures:** For a specific business project managed jointly with a client.

### 8.1.2 Mandatory Written Agreement and Signatory Requirements

Because a joint account is not a client account in the firm's sole name, the standard SRA Accounts Rules do not fully apply. However, this does not mean it's unregulated.

#### Requirements

1. **Written agreement:** A clear agreement must be in place between all parties, outlining the purpose of the account and the operational rules (e.g., whether one or two signatures are required for withdrawals).
2. **Signatory safeguards:** To mitigate the risk of the other party misusing funds, it is strongly recommended that the account operates on a dual-signature basis, requiring both the solicitor and the other party to authorize transactions. This upholds the solicitor's duty to safeguard money.

### 8.1.3 Accounting for Joint Account Transactions

While the money in a joint account is client money, it bypasses the firm's main client account. Therefore, the firm's accounting records are different.

The firm must still:

- Obtain bank statements for the joint account at least every five weeks.
- Keep a central record of all bills issued.
- Maintain a record of transactions related to the matter.

However, the detailed client ledger and cash book entries required for the main client account are not necessary. The primary record becomes the joint account's own bank statements.

## 8.2 Operation of a Client's Own Account

### 8.2.1 When is it Permissible? (Lack of Capacity, Security, etc.)

This occurs when a solicitor is given the authority to operate a bank account that is in the client's own name. This is typically done to protect vulnerable clients.

#### Common Scenarios

- **Powers of attorney:** Acting as an attorney under a registered Lasting or Enduring Power of Attorney.
- **Court of protection deputyship:** Being appointed by the court to manage the financial affairs of someone who lacks mental capacity.
- **Specific security arrangements:** Where a lender requires a solicitor to control the flow of loan funds directly from the borrower's account.

### 8.2.2 The Firm's Rights and Responsibilities as Signatory

The solicitor steps into the shoes of the client for the purpose of managing the account. Their responsibilities are immense:

- **Fiduciary duty:** They must act in the client's best interests at all times.
- **Stewardship:** They must manage the funds prudently and keep detailed records of all income and expenditure.
- **Segregation:** They must never mix these funds with firm or other client money.

### 8.2.3 Record-Keeping and Accounting Obligations

The SRA Rules are slightly modified for this arrangement. The firm must:

1. Obtain bank statements at least every five weeks.

2. Reconcile the account (compare its own records to the bank statement) at least every five weeks.
3. Keep a readily accessible central record of bills.
4. Maintain its own internal record of all transactions it conducts on the account.

The challenge is obtaining statements every five weeks, which can be difficult with some high-street banks. If impossible, the firm must document the steps taken to ensure the client's money is safe.

### 8.3 Third-Party Managed Accounts (TPMAs) - The Deep Dive

A Third-Party Managed Account (TPMA) is a modern alternative to the traditional client account. Instead of the law firm holding client money in its own bank account, it uses a specialized, regulated third-party service to hold and control the funds.

Think of it like this:

**For traditional client account:** You are the banker. You receive the money, you hold it in your vault (your client account), and you pay it out according to your instructions.

**For TPMA:** You are the architect. You design the payment plan (the transaction), but a specialized construction company (the TPMA provider) holds all the materials (the money) and makes the payments exactly according to your blueprints. You never touch the bricks and mortar yourself.

#### 8.3.1 Definition and Regulatory Status

A TPMA is an account, provided by an FCA (Financial Conduct Authority) authorised payment institution, which is used to hold money for a specific client matter. The law firm instructs the provider, but the provider holds the money and executes the payments.

#### Regulatory Status

This is the most critical concept to grasp. The SRA Accounts Rules define client money as money "held or received by" the firm.



With a TPMA, the firm never physically holds or receives the money. The client sends funds directly to the TPMA provider. Therefore, the money in a TPMA is not legally classified as "client money" for the purposes of the SRA Accounts Rules.

### **Implication**

Because it's not client money, the firm is exempt from the core requirements of the *Rules*, such as:

- The need to have a client bank account at all.
- The obligation to pay client money into a client account promptly.
- The requirement to perform five-weekly client account reconciliations.

The TPMA provider is regulated by the Financial Conduct Authority (FCA), not the SRA.

### **8.3.2 The Mechanics: How a TPMA Works in Practice**

Let's walk through a typical property transaction using a TPMA:

1. **Instruction and setup:** The firm instructs the TPMA provider to set up a dedicated account for "Client A's purchase of 1 High Street." The provider gives unique bank details for this specific transaction.
2. **Funding:** The firm tells the client and the client's lender to send all funds directly to the TPMA account details provided.
3. **Holding:** The TPMA provider holds the funds. The law firm cannot access this money directly.
4. **Authorizing payments:** When a payment is due (e.g., on completion), the law firm logs into the TPMA portal and instructs the provider to pay "£250,000 to the seller's solicitor."
5. **Execution:** The TPMA provider executes the payment directly from the TPMA. The money never passes through the law firm's bank accounts.

6. **Final distribution:** After completion, the firm instructs the provider to pay the estate agent's commission and any surplus funds back to the client.

Throughout this process, the law firm directs but does not disburse.

### 8.3.3 Firm's Duties: A Shift from Handler to Supervisor

Using a TPMA does not mean the firm has no duties. The duties simply shift from being a handler of money to being a supervisor of the process. The firm's core fiduciary duty to act in the client's best interests remains absolute.

#### 1. Rigorous Due Diligence on the Provider

The firm cannot use any random service. It must ensure the TPMA provider is:

- FCA-Authorised: It must be an Authorised Payment Institution (API) or a Small Payment Institution with equivalent safeguarding.
- Financially Stable.
- Technologically Secure: Its systems must be robust against cybercrime.
- Insured: It should have adequate insurance to protect client funds.

#### 2. Full and Informed Client Consent

The firm must have a clear, written conversation with the client, explaining: "Your money will not be held in our statutory protected client account. It will be held by [TPMA Provider Name], which is regulated by the FCA, not the SRA."

The firm is to explain the FCA's safeguarding rules and any applicable financial services compensation schemes. The protections are different, not necessarily worse, but the client must understand this.

The explanation must also detail how payments will be made into and out of the TPMA and specify who will bear the provider's fees, whether the firm or the client.

#### 3. Robust Operational Oversight and Record-Keeping

- **Audit trail:** The firm must keep a detailed record of all instructions sent to the TPMA provider. This is your evidence of what was supposed to happen.

- **Reconciliation** (of a different kind): While you don't reconcile a bank statement, you must regularly check the TPMA portal statements against your own internal records to ensure all instructions have been carried out correctly and all funds are accounted for.
- **Internal systems:** The firm must have clear internal policies on when and how TPMAs are used.

## 8.4 Property Transactions: A Practical Application

### 8.4.1 Stakeholder Money: The Special Rules for Deposits

In a property transaction, the buyer's deposit is often held by the seller's solicitor as "stakeholder." This means the solicitor holds the money neutrally for *both* parties until completion. It does not belong to the seller until that point.

#### Accounting Treatment

The clearest method is to record the deposit on a separate ledger account, e.g., "Stakeholder - A Buyer & B Seller."

- **On Receipt:** Debit (Dr) Client Bank Account; Credit (Cr) Stakeholder Ledger Account.
- **On Completion:** The money is released to the seller. Debit (Dr) Stakeholder Ledger Account; Credit (Cr) Seller's Client Ledger Account.

### 8.4.2 Accounting for Mortgage Advances from a Lender

When acting for both the buyer and the lender, the mortgage advance presents a question: who is the money held for before completion?

#### Best Practice (Clear Audit Trail)

1. On receipt, credit the money to a ledger in the lender's name (e.g., "ABC Bank Ltd - Mortgage for Client X").
2. On the day of completion, perform an inter-client transfer from the lender's ledger to the buyer's ledger.

3. The money is then used from the buyer's ledger to complete the purchase.

This method perfectly tracks the change in beneficial ownership of the funds.

### **8.4.3 Accounting for Mortgage Redemptions on Sale**

When acting for a seller who has a mortgage, part of the sale proceeds must be used to pay off the existing lender.

#### **Best Practice**

1. Receive the entire sale proceeds and credit them to the seller's client ledger.
2. Immediately perform an inter-client transfer of the mortgage redemption amount from the seller's ledger to a ledger in the lender's name (e.g., "XYZ Building Society - Redemption for Seller Y").
3. Pay the redemption money to the lender from this ledger.

This provides a transparent record showing that the lender's share of the proceeds was identified and ring-fenced immediately.

## **8.5 Conclusion**

Alternative client money arrangements demand the same level of diligence and ethical conduct as traditional client accounts, even where regulatory responsibilities differ. Whether through joint accounts, client-operated accounts, or TPMAs, solicitors must maintain rigorous oversight, accurate documentation, and transparent communication to preserve the integrity of client funds.

Ultimately, these mechanisms reflect the evolving landscape of legal financial management, where technology, regulation, and trust converge. By applying sound judgment, adhering to professional standards, and documenting every transaction with precision, firms reinforce their commitment to accountability and the protection of client interests.

# 9

## COMPLIANCE, REPORTING, AND RECORD RETENTION

The annual accountant's report is a cornerstone of financial accountability within legal practice. It provides independent assurance to the Solicitors Regulation Authority (SRA) that firms are handling client money responsibly and in full compliance with the Accounts Rules. Beyond being a regulatory formality, the report serves as an essential safeguard for client protection, ensuring transparency, integrity, and adherence to fiduciary duties. The chapter outlines when reports are required, the scope of the reporting accountant's role, and the firm's duties in cooperating fully with this independent review.

It also examines the broader compliance environment, from maintaining accurate records and reconciling accounts to implementing cybersecurity measures and preparing for potential SRA audits. By treating the reporting process as a continuous practice rather than a yearly obligation, firms can identify weaknesses early, strengthen internal controls, and maintain the high professional standards expected of the legal profession.

### **9.1 The Annual Accountant's Report: Purpose and Triggering Events**

Think of the Annual Accountant's Report as a mandatory "MOT test" for your firm's financial health and compliance. Its primary purpose is to provide independent assurance to the SRA that you are handling client money correctly and that it is safe.

You **MUST** obtain a report if, at any time during your accounting period, you:

- Held or received client money in a general or designated client account.
- Operated a joint account as a signatory.
- Operated a client's own account as a signatory.

### **Exception**

You are exempt from obtaining a report if the only client money you handled was from the Legal Aid Agency OR if the total balance on all your client, joint, and client's own accounts never exceeded an average of £10,000 and a maximum of £250,000 at any one time during the period.

## **9.2 The Role of the Reporting Accountant: Scope of the Engagement**

The Reporting Accountant is an independent, qualified professional (a registered auditor) hired to conduct this "MOT." They are not your enemy; they are a crucial part of the profession's regulatory safety net.

Their job is not to audit every transaction but to perform specific tests and procedures to obtain reasonable assurance that:

1. You have complied with the SRA Accounts Rules throughout the period.
2. Client money has been kept safe and is properly accounted for.

They will test your reconciliations, sample client ledgers, check authorization of payments, and verify that your systems and controls are adequate.

## **9.3 The Firm's Obligations: Obtaining, Delivering, and Cooperating**

Your responsibilities in this process are active and strict:

1. **Obtain the report:** You must instruct a suitable accountant to prepare the report within six months of the end of your accounting period.

2. **Cooperate fully:** You must provide the accountant with all information and documents they require. This is not optional. Withholding information is a serious breach.
3. **Deliver the report to the SRA:** You must submit the report to the SRA only if it is qualified.

### What is a "Qualified Report"?

A report is qualified if the accountant finds a breach of the Rules that puts, or has put, client money at risk. An unqualified ("clean") report does not need to be sent to the SRA.

## 9.4 Common Qualifying Conditions and What They Mean

A qualification is a major "red flag." Common reasons for a qualified report include:

1. **Client account shortfall:** Money belonging to other clients has been used, creating an overdrawn client ledger. This is one of the most serious qualifications.
2. **Failure to reconcile:** Not performing the mandatory five-weekly reconciliations.
3. **Improper use as a banking facility:** Using the client account for payments unrelated to legal transactions (breach of *Rule 3.3*).
4. **Systemic billing issues:** Routinely billing for costs not yet incurred and transferring the money to the office account, putting client money at risk.
5. **Significant deficiencies in records:** Accounting records are missing, inaccurate, or incomplete.

A pattern of qualified reports will almost certainly trigger an SRA investigation.

## 9.5 Storage of Accounting Records: The Six-Year Rule

You must keep your accounting records safe and accessible for at least six years from the date of the last transaction on the record.

## **What Constitutes "Accounting Records"?**

It's a broad definition, that includes:

- Client ledgers and cash books.
- Bank statements and paying-in slips.
- Copies of bills and other written notifications of costs.
- Chequebooks (used and unused).
- Reconciliation reports.
- Accountants' reports.

This ensures a clear audit trail exists long after a matter has concluded, which is vital for resolving any future disputes or investigations.

## **9.6 Format of Stored Records: Originals, Scanned Copies, and Legibility**

The SRA is technology-neutral. Records can be stored either in their original paper form or as scanned electronic copies.

If you choose to scan records, you **MUST** ensure:

- The copy is a complete and accurate replica of the original.
- The scanning process is secure and reliable.
- The records remain legible and accessible for the entire six-year retention period. This means having a plan for software and hardware obsolescence (e.g., can you still read that file type in 5 years?).

## **9.7 Destruction of Records: Timing and Process after the Retention Period**

After the six-year retention period has expired, you may destroy the records.



## Best Practice for Destruction

1. **Have a clear policy:** Define how and when records will be destroyed.
2. **Destroy securely:** Paper records should be confidentially shredded. Electronic records should be permanently deleted so they cannot be recovered.
3. **Do not destroy early:** The six-year clock starts from the last transaction on the file. Do not be tempted to destroy records early to save space.

## 9.8 Data Protection and Cybersecurity Considerations for Client Financial Data

Your accounting records contain highly sensitive personal and financial data. You have a legal duty under data protection law (*UK General Data Protection Regulation*) to protect it.

### Key Actions

1. **Physical security:** Lock filing cabinets and secure office premises.
2. **Cybersecurity:** Use firewalls, encryption, multi-factor authentication, and regular security training for staff to prevent phishing attacks.
3. **Access controls:** Ensure only authorized staff can access accounting records and systems.
4. **Breach plan:** Have a plan to respond to a data breach, including notifying the ICO and affected individuals if necessary.

A data breach of your accounts file is both a data protection failure and a breach of your duty to keep client affairs confidential.

## 9.9 Preparing for an SRA Audit or Investigation

The SRA has the power to conduct a routine visit or a targeted investigation. The best preparation is ongoing, good practice. Your "Always Ready" Checklist:

1. **Organised records:** Your accounting records (both physical and digital) are well-ordered and can be produced quickly.
2. **Up-to-date reconciliations:** Your last client account reconciliation is current and correct.
3. **Breach register:** Your breach register is maintained and shows a culture of identifying and correcting errors.
4. **Policies and procedures:** You have written, implemented policies for handling client money, interest, and breaches.
5. **COFA engagement:** Your COFA is fully informed and involved in the firm's financial compliance.
6. **Staff training records:** You can demonstrate that relevant staff have been trained on the Accounts Rules.

If the SRA knocks, cooperation, transparency, and well-kept records are your greatest assets. Trying to hide a problem will always make the outcome worse.

## 9.10 Conclusion

The accountant's report, together with robust record-keeping and security practices, demonstrates a firm's commitment to ethical and regulatory compliance. A well-prepared firm views the report not as an external test but as a reflection of its internal integrity and operational discipline. Compliance with storage, retention, and data protection requirements further reinforces public confidence that client money and information are safeguarded at all times.

Ultimately, effective cooperation with reporting accountants, strict adherence to the six-year record retention rule, and readiness for SRA inspections form the backbone of a sound compliance culture. Firms that maintain accurate records, monitor breaches transparently, and foster accountability across all staff not only meet regulatory expectations but also enhance their professional reputation and client trust.

# APPENDIX A

## The Solicitor's Daily Accounting Mantra

**CORE PRINCIPLE:** For every transaction, one account gets a DEBIT, another gets a CREDIT. The amounts must be equal. Also remember the general rule “Debit the receiver, Credit the giver”

### I. Receiving Money

#### 1. Receiving CLIENT MONEY (e.g., on account of costs):

When the solicitor receives money from the client:

- The client is the giver (they're giving money to the solicitor to hold).
- The solicitor's client bank account is the receiver (money is coming in).

Therefore, you:

- DEBIT Client Bank Account
- CREDIT Client's Ledger Account (Client Column)

#### 2. Receiving OFFICE MONEY (e.g., payment of your bill):

- DEBIT Office Bank Account
- CREDIT Client's Ledger Account (Business Column)

#### 3. Receiving a MIXED payment (whole amount into client account first):

- DEBIT Client Bank Account (for full amount)
- CREDIT Client's Ledger Account (Client Column - for full amount)
- Then transfer the office portion out PROMPTLY.

## II. PAYING MONEY

4. Paying from CLIENT ACCOUNT (for a client's expense):

- DEBIT Client's Ledger Account (Client Column)
- CREDIT Client Bank Account

5. Paying from OFFICE ACCOUNT (for a client, creating a debt):

- DEBIT Client's Ledger Account (Business Column)
- CREDIT Office Bank Account

## III. FEES AND BILLING

6. Issuing a BILL to a client (no cash moves):

- DEBIT Client's Ledger Account (Business Column) [Total inc. VAT]
- CREDIT Profit Costs Account [Fees only]
- CREDIT HMRC VAT Account [VAT amount]

7. Transferring money from CLIENT to OFFICE account to pay your bill:

- DEBIT Client's Ledger Account (Client Column)
- CREDIT Client Bank Account
- DEBIT Office Bank Account
- CREDIT Client's Ledger Account (Business Column)

8. Reducing a bill (ABATEMENT):

- DEBIT Profit Costs Account [Reduction in fees]
- DEBIT HMRC VAT Account [Reduction in VAT]
- CREDIT Client's Ledger Account (Business Column) [Total reduction]

## IV. TRANSFERS

9. CASH TRANSFER (money moves between bank accounts):

- From the account it LEAVES: CREDIT [Bank Account]
- From the account it ENTERS: DEBIT [Bank Account]
- ...with corresponding ledger entries.

10. INTER-CLIENT TRANSFER (money stays in client account, owner changes):

- DEBIT Client A Ledger (Client Column)
- CREDIT Client B Ledger (Client Column)

## **V. DISBURSEMENTS**

11. Paying a TRUE DISBURSEMENT (Agency Method - invoice to client):

- DEBIT Client's Ledger Account (Client Column) [Total amount]
- CREDIT Client Bank Account [Total amount]

12. Paying a RECHARGE (Principal Method - invoice to firm):

- DEBIT Client's Ledger Account (Business Column) [Net cost]
- DEBIT HMRC VAT Account [VAT paid]
- CREDIT Office Bank Account [Total paid]

## **VI. INTEREST**

13. Bank pays interest into GENERAL CLIENT ACCOUNT (firm keeps it):

- DEBIT Office Bank Account
- CREDIT Interest Received Account

14. Firm pays interest to a CLIENT from OFFICE ACCOUNT

- DEBIT Interest Payable Expense Account
- CREDIT Office Bank Account

## VII. RECTIFYING BREACHES

15. Correcting an OVERDRAWN CLIENT LEDGER (injecting office money):

- DEBIT Client's Ledger Account (Client Column)
- CREDIT Client Bank Account
- DEBIT Office Bank Account
- CREDIT Client's Ledger Account (Business Column)

16. Writing off a BAD DEBT:

- DEBIT Bad Debts Expense Account
- CREDIT Client's Ledger Account (Business Column)

**Recite this Daily:** Let the DEBIT and CREDIT flow become second nature.

**Remember:** LEFT is DEBIT, RIGHT is CREDIT. For every action, there is an equal and opposite accounting entry.

# APPENDIX B

## SAMPLE ACCOUNTING RECORDS

These sample forms are essential tools for complying with the SRA Accounts Rules. They provide a clear and organised method for tracking every transaction and ensuring the integrity of your client money records.

### B.1: Sample Client Ledger

A client ledger is a record of all financial activity for a single client matter. You must have a separate ledger for each client matter.

#### Key for Students

- Dr (Debit) for Client Account: Money coming into the client account.
- Cr (Credit) for Client Account: Money going out of the client account.
- The goal is for the client ledger to eventually reach a zero balance, showing all money has been properly applied or returned.
- Notice how the office account column is only used when money is transferred out of client account as a paid fee.

### B.2: Sample Three-Part Cashbook

The three-part cashbook is the firm's central record of *all* transactions through the client and office bank accounts on a daily basis. It's called "three-part" because it reconciles the client bank account, the office bank account, and the individual client ledgers.

## Three-Part Cashbook - Client Bank Account (Extract)

Date	Details	Chq No	Client Bank Account	Client Ledger Folio	
			Dr (In)	Cr (Out)	
01/04/2024	Smith, John - Money on account		£2,500.00		SL-1
05/04/2024	Anytown Council - Local Search	1001		£350.00	SL-1
10/04/2024	Transfer to Office Account (Fee INV-001)	1002		£1,200.00	SL-1 / O-1
15/04/2024	Smith, John - Mortgage Funds		£150,000.00		SL-1
20/04/2024	Jones & Co - Completion Monies	1003		£151,000.00	SL-1
25/04/2024	Jones & Co - Surplus Funds		£450.00		SL-1
30/04/2024	Smith, John - Refund	1004		£398.75	SL-1
30/04/2024	Smith, John - Interest	1005		£12.25	SL-1



30/04/ 2024	Total for April		£152,950.0 0	£152,961.0 0	
	Balance c/f			£11.00	

**Explanation:** The cashbook shows the actual bank balance is £11.00. The reconciliation process will now identify what this £11.00 represents (e.g., an unrepresented cheque).

### B.3: Sample Bank Reconciliation Statement

This is done at the end of each month to explain the difference between the balance in your cashbook and the balance on the bank statement.

#### Bank Reconciliation Statement (As at 30 April 2024)

Description	Amount
Cashbook Balance (Client Account) at 30/04/2024	(£11.00)
<i>Add: Unpresented Cheques (cheques issued but not yet cashed by the recipient)</i>	
Cheque 1004 - J Smith (Refund)	£398.75
Cheque 1005 - J Smith (Interest)	£12.25
Total Unpresented Cheques	£411.00
<i>Less: Lodgements not yet credited (Money paid in but not yet showing on bank statement)</i>	

None	£0.00
Adjusted Balance	£400.00
Bank Statement Balance at 30/04/2024	£400.00

### **B.4: Sample Client Ledger Reconciliation (List of Balances)**

This proves that the total of all the individual client ledger balances equals the balance on the client cashbook.

#### **Client Ledger Reconciliation (List of Balances) (As at 30 April 2024)**

Client Matter Ledger	Ledger Reference	Balance
Smith, John - Property Purchase	SL-1	£0.00
Patel, Amita - Will Dispute	SL-2	£1,500.00
Davis, Co - Commercial Lease	SL-3	£5,250.00
Williams, T - Matrimonial	SL-4	(£250.00) *
Total of All Client Ledger Balances		£6,500.00
Less: Client Account Liabilities (e.g., unpresented cheques from B.3)		(£411.00)
Adjusted Client Ledger Total		£6,089.00
Balance per Client Cashbook at 30/04/2024		£6,089.00

# APPENDIX C

## Summary of Essential Accounting Entries

This quick-reference guide shows the fundamental double-entry bookkeeping transactions under the SRA Accounts Rules.

Key:

- CA = Client Account
- OA = Office Account
- CL = Client Ledger
- WIP = Work in Progress
- BP = Bills Payable

### 1. Receiving Client Money

**Scenario:** Client sends £5,000 as advance payment.

Account	Debit	Credit
CA	5,000	
CL - Client		5,000
Receipt of money on account		

## 2. Paying Agency Disbursement

**Scenario:** Pay £500 court fee from client account.

Account	Debit	Credit
CL - Client	500	
CA		500
Payment of court fee		

## 3. Raising a Bill

**Scenario:** Bill client £2,000 (£1,500 costs + £500 disbursement).

Account	Debit	Credit
CL - Client	2,000	
BP		2,000
Bill for costs & disbursements		

## 4. Transfer for Paid Bill

**Scenario:** Pay bill from client account funds.

Account	Debit	Credit
BP	2,000	

CL - Client		2,000
Settle bill from funds		

Account	Debit	Credit
OA	2,000	
CA		2,000
Transfer to office account		

## 5. Principal Disbursement

**Scenario:** Pay £50 courier from office account.

Account	Debit	Credit
Disbursements	50	
OA		50
Courier charges		

## 6. Paying Interest

**Scenario:** Pay £25 interest to client.

Account	Debit	Credit
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OA	25	
CL - Client		25
Interest payment		

## 7. Correcting Breach

**Scenario:** Office cheque £1,000 wrongly in client account.

Account	Debit	Credit
OA	1,000	
CA		1,000
Correct      erroneous payment		

# APPENDIX D

## SRA Accounts Rules 2019 (Key Extracts)

Source: *SRA Standards and Regulations, SRA ACCOUNTS RULES 2019*

These *Rules* set out the requirements for keeping and maintaining client money. The purpose of these *Rules* is to keep client money safe. You must comply with the principles set out in the *SRA Standards and Regulations* in relation to your practice, including your handling of client money.

### **Rule 2: Client Money and Client Accounts**

2.1 You ensure client money is paid promptly into a client account.

2.2 You ensure that client money is held in a client account at a bank or building society authorised by the Prudential Regulation Authority.

2.3 You only withdraw client money from a client account:

(a) for the purpose for which it is being held, or

(b) following receipt of instructions from the client, or the third party for whom the money is held.

### **Rule 3: Use of a Client Account**

3.1 You do not use a client account to provide banking facilities to clients or third parties. Payments into, and transfers or withdrawals from, a client account must be in respect of the delivery by you of regulated services.

**Rule 4: Duty to Report Breaches**

4.1 You report promptly to the SRA any serious breach of these Rules, or any serious failure to comply with these Rules, and take any necessary steps to address any resulting issues.

**Rule 5: Accounting Systems and Records**

5.1 You keep and maintain written accounting records of your practice to show accurately the position with regard to:

- (a) the money held for each client and third party, and
- (b) any other money dealt with through a client account.

5.2 You keep and maintain:

- (a) all accounts, including client ledgers, and
- (b) a record of all bills of costs and other written notifications of costs.

5.3 You keep and maintain a record of all reconciliations.

**Rule 6: Reconciliations**

6.1 You at least every five weeks:

- (a) compare the balance on the client ledger with the balance on the client account, and
- (b) prepare a reconciliation statement.

6.2 You investigate and resolve any differences shown by the reconciliation.

**Rule 7: Duty to Correct Breaches**

7.1 You correct any breaches of these Rules promptly upon discovery.

**Rule 8: Interest**

8.1 You account to clients or third parties for a fair sum of interest on any client money held by you on their behalf.



**Rule 9: Accounting for Costs**

9.1 You only withdraw your costs from client money if:

- (a) you have given a bill of costs or other written notification of costs to the client or the paying party, and
- (b) the client or the paying party has been notified that the money held will be used for payment of the costs.

**Rule 10: Client Money Withheld**

10.1 You return client money to the client promptly, as soon as there is no longer any proper reason to hold those funds.

**Rule 11: Outsourcing**

11.1 If you use a third party to carry out any function under these Rules, you remain accountable for the work done and ensure that the third party complies with these Rules.

**Important Note:** These are key extracts from the SRA Accounts Rules 2019 and are not exhaustive. The full Rules contain additional provisions, guidance and exceptions

## Master the Principles and Practice of Client Money Management for the SQE1

*Law Angels SQE Series: Solicitors Accounts* provides a clear, comprehensive, and practical guide to the Solicitors Accounts Rules (SAR). Meticulously designed for the SQE1 curriculum, this textbook moves beyond theory to cultivate the precise, procedural, and ethical skills essential for the correct handling of client money.

Inside, you will find:

- **Foundational Principles:** A clear explanation of the core principles underpinning the SAR, including the fundamental duty to protect client money and the key distinctions between client and office money.
- **Rule-Based Application:** A step-by-step guide to the rules governing the receipt and payment of client money, the operation of client and office accounts, and the treatment of mixed receipts.
- **Accounting in Practice:** Practical guidance on maintaining proper accounting records, performing the three-way client bank reconciliation, and understanding the types of transactions that pass through the client account.
- **Interest Calculations:** A straightforward approach to calculating and paying interest on client money in compliance with the SRA principles.
- **Risk and Compliance:** Essential coverage of a solicitor's duties, including the consequences of breaches, the SRA's enforcement powers, and the importance of internal systems and controls.
- **Exam-Focused Approach:** Worked examples, ledger illustrations, and scenario-based problems designed to build your confidence and proficiency in tackling SQE-style account questions.

This book is more than a textbook, it is an essential manual for financial compliance that empowers you to manage client funds with accuracy and integrity. It is the definitive resource for any candidate seeking not just to pass the SQE1, but to build a solid foundation for a reputable and compliant legal practice.

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