IOLTA Litigation Update: Reviewing the Brown Decision; Texas Case Remanded

by Bev Groudine

The Spring issue of Dialogue brought news of the Supreme Court’s decision in Brown v. Legal Foundation of Washington, 538 U.S. ___, (2003), which was issued shortly before press time. Dialogue now offers a closer look at the details of the Court’s decision, as well as its subsequent order remanding Phillips v. Washington Legal Foundation, 02-01, back to the Fifth Circuit Court of Appeals.

On March 26, 2003, the U.S. Supreme Court issued its decision in Brown v. Legal Foundation of Washington, upholding the constitutionality of IOLTA under the Just Compensation Clause of the Fifth Amendment. Justice Stevens authored the 5-4 majority decision, which Justices O’Connor, Souter, Ginsburg and Breyer joined. In its ruling the Court held that even assuming that the interest generated on IOLTA accounts amounted to a per se taking, such a taking was for a valid public use and the amount of just compensation due was zero. As a result, the Court found that the operation of the IOLTA program in Washington does not violate the Fifth Amendment.

**IOLTA a public use**

The Court’s analysis began by setting forth that the text of the Fifth Amendment “confirms the state’s authority to confiscate private property”, so long as two conditions are met: “the taking must be for a ‘public use’ and ‘just compensation’ must be paid to the owner.” The Court quickly disposed of the ‘public use’ question by stating that “…the overall, dramatic success of these programs in serving the compelling interest in providing legal services to literally millions of needy Americans certainly qualifies the Foundation’s distribution of these funds as a ‘public use’ within the meaning of the Fifth Amendment.”

The Court then discussed the type of “taking,” if any, involved in the case. Petitioners alleged two takings claims based on, first, the requirement that certain types of client funds be placed in an IOLTA account and, second, the transfer of interest from an IOLTA account to the Washington IOLTA program. Applying a regulatory taking analysis, the Court concluded that the placement of funds in an IOLTA account was not a taking “because the transaction had no adverse economic impact on petitioners and did not interfere with any investment-backed expectations.” As to the alleged taking of interest, the Court indicated that the per se analysis was appropriate to the facts of this case and consistent with the finding in Phillips that the interest is the property of the clients. The majority assumed that the petitioners’ “interest was taken for a public use when it was ultimately turned over to the Foundation.” This assumption, however, did not end the Court’s inquiry.

**No just compensation due**

The Court held that, in any event, there was no constitutional violation because no just compensation was due. In essence, the Court found that the plaintiffs in the case lost nothing of value given the fact that transaction costs would have outweighed the small amount of gross interest their individual accounts would have earned. In reaching its conclusion, the Court applied a long line of Fifth Amendment cases on just compensation, stating: “[J]ust compensation required by the Fifth Amendment is measured by the property owner’s loss rather than the government’s gain.”

Finally, the Court addressed the plaintiffs’ argument that funds could have mistakenly been deposited in an IOLTA account when the interest generated would actually have exceeded the transaction costs involved, contrary to the law establishing the IOLTA program in Washington State. While recognizing that mistakes might occur, the Court pointed out that the responsibility for ensuring that only qualifying funds are deposited in IOLTA accounts rests with the entity making the deposits (in this case the limited practice officers handling real estate escrows). While the property owner might

(continued on page 7)
Litigation Update
(continued from page 6)

have a claim against the entity making a faulty deposit, that faulty deposit would not involve any state action subject to Fifth Amendment protection.

The dissents
Justice Scalia authored a spirited dissent, which was joined by Chief Justice Rehnquist and Justices Kennedy and Thomas. In it, IOLTA was likened to a “Robin Hood Taking, in which the government’s extraction of wealth from those who own it is so cleverly achieved, and the object of the government’s larcenous beneficence is so highly favored by the courts (taking from the rich to give to indigent defendants) that the normal rules of the Constitution protecting private property are suspended.” Justice Scalia argued that the fair market value of the interest earned by the clients’ principal should be the test of just compensation, rather than the net interest approach used by the majority.

Justice Kennedy also issued a brief additional dissent in which he raised First Amendment concerns regarding IOLTA. Kennedy wrote: “The First Amendment consequences of the State’s action have not been addressed in this case, but the potential for a serious violation is there. . . One constitutional violation (the taking of property) likely will lead to another (compelled speech).”

Texas case
Shortly after the Court granted certiorari in the Brown case in 2002, the Texas IOLTA program filed a petition for certiorari in its case, Phillips, et al v. Washington Legal Foundation, 02-1. That petition was filed following the denial of a petition for en banc

From the Chair...
(continued from page 3)

force will gather and provide information on the issues that have been the subject of IOLTA rule changes in recent years to increase IOLTA revenue so that programs can determine what other, if any, changes they may want to explore. I expect the task force will issue a preliminary report in San Francisco.

Ideas for action by programs include the following:
• Conversion – This is a good time for programs that have either voluntary or opt-out attorney participation to consider converting their programs to opt-out or mandatory status. Increasing attorney participation by converting a program’s status is one of the most effective ways to increase IOLTA revenue. ABA policy has supported converting to mandatory status since 1988. More importantly, the Brown ruling has put to rest concerns that mandatory IOLTA violates the Fifth Amendment.
• Fundraising – Highlighted on the cover of this issue of Dialogue, as well as in two previous editions, is the role that IOLTA programs can play in developing new sources of funding for civil legal assistance. The cover story focuses on the importance of IOLTA in statewide funding initiatives, whether the new funds are administered by IOLTA programs or other access-to-justice organizations. The recent successes in Arizona, Illinois, New Hampshire and Pennsylvania show that when they engage in statewide funding efforts, IOLTA programs can secure impressive gains. (The efforts in these four states will raise millions of dollars for legal services.)
• Banking relationships – Even in this dreary interest rate climate, attention to banking matters remains an essential part of any program’s operations. Amending rules to require banks to treat IOLTA accounts with parity may help shore up IOLTA revenues. As banks consolidate and become regional or national entities, communication and coordination between IOLTA programs is becoming a necessary counterweight and a means to help gain more favorable treatment of IOLTA accounts across state lines.

We will delve into these last two issues regarding banks when the IOLTA community meets for the Summer IOLTA Workshops. Other sessions will address loan repayment and assistance programs, grant making, grantee evaluation, funding racial justice initiatives, and legal needs assessments. In addition, the workshops offer an excellent opportunity for informal discussions about other topics of interest. I hope you plan to attend—this is an important time for IOLTA.
Litigation Update
(continued from page 7)

review of a ruling against the Texas IOLTA program issued by a three-judge panel of the Fifth Circuit Court of Appeals, which found that IOLTA violated the Fifth Amendment. On March 31, 2003, the Supreme Court granted the certiorari petition, vacated the decision of the Fifth Circuit, and remanded the case to the Fifth Circuit “for further consideration in light of Brown.”

What’s next?
First Amendment claims were raised in the original complaints filed in the Texas and Washington cases. While the lower courts have in part addressed those claims, whether the plaintiffs in either case will pursue the issue further in light of the Brown decision remains an open question.

In the Washington litigation, the Ninth Circuit Court of Appeals, after ruling that no Fifth Amendment violation existed, remanded the First Amendment issue to the district court to consider “what speech, if any, is at issue and whether the IOLTA program violates any rights Appellants may have emanating from the First Amendment.” In the Texas case, the district court found no violation of the First Amendment following a bench trial, and dismissed the claim. The Fifth Circuit, finding that a Fifth Amendment violation existed, decided that it did not need to address the First Amendment claim. Thus, while the First Amendment issue may be on a faster track in the Fifth Circuit, only time will tell if and when it will be further litigated.

Regardless of whether more litigation awaits IOLTA programs, the Brown decision is an important victory, both for affirming such a critical source of funding for legal services, and for recognizing the compelling importance of legal services for the poor. As American Bar Association President Alfred P. Carlton, Jr. stated: “The real beneficiaries of this ruling are the tens of thousands of poor people who receive legal assistance because of IOLTA.”

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IOLTA Leadership
(continued from page 5)

New Hampshire
For many IOLTA programs, the first step into statewide resource development efforts has been, as it was in Arizona, through a state legislative campaign. The New Hampshire Bar Foundation, the state’s IOLTA program, took a different route. In 1996 the bar foundation and its former executive director Tina Abramson sought to increase revenues significantly by embarking on an ambitious planned giving and major gifts campaign to increase its endowment. By 2000, the foundation generated $1 million, half in cash gifts and half in bequests, which is quite a success for a state with only 3,000 lawyers. The success of this effort led to a decision to develop a statewide annual private bar campaign, to be coordinated and directed by bar foundation staff, to raise regular operating funds for the three legal aid programs. The Campaign for Legal Services officially kicked off at the bar foundation’s annual dinner in June 2002 with $300,000 in leadership gifts from firms pledging to donate at the rate of $500 per lawyer. The campaign is expected to reach its three-year goal of $750,000.

In these states as well as others, the role of IOLTA programs and their directors in initiating, organizing, coordinating and managing state-level resource development work has led to substantial increases in funding for legal aid programs. Opportunities exist in other states, where there is insufficient state-level person power, for IOLTA personnel to step in and either fill a void or complement the work being done by others. In some states, active participation and leadership by IOLTA programs and their staff may be a necessity if access to justice is to be improved.

The ABA Project to Expand Resources for Legal Services (PERLS) offers assistance regarding state and local efforts to develop new sources of legal services funding. For more information, contact the author of this article, Meredith McBurney, at 303-329-8091 or via email at mm8091@aol.com

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