

**PENNSYLVANIA INTEREST ON LAWYERS
TRUST ACCOUNT BOARD**

FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION
YEARS ENDED JUNE 30, 2005 AND 2004
AND
INDEPENDENT AUDITOR'S REPORT



PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Pennsylvania Interest on Lawyers Trust Account Board
Harrisburg, Pennsylvania

We have audited the accompanying basic financial statements of the Pennsylvania Interest on Lawyers Trust Account Board, a component unit of the Supreme Court of the Commonwealth of Pennsylvania, as of and for the years ended June 30, 2005 and 2004, as listed in the table of contents. These financial statements are the responsibility of the Board's management. Our responsibility is to express an opinion on these financial statements based on our audits.

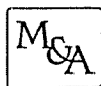
We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Pennsylvania Interest on Lawyers Trust Account Board as of June 30, 2005 and 2004, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 3 to 11 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

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Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information on pages 23 through 26 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information, except for the portion marked "unaudited," on which we express no opinion, has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

McKonly & Asbury, LLP

Harrisburg, Pennsylvania
August 23, 2005

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

INTRODUCTION

The following discussion and analysis of the financial performance and activity of the Pennsylvania Interest on Lawyers Trust Account Board (IOLTA Board) is to provide an introduction and understanding of the basic financial statements of the IOLTA Board for the fiscal years ending June 30, 2005 and 2004. This discussion has been prepared by management and is unaudited; and should be read in conjunction with the financial statements and their notes, which follow this section.

An Interest on Lawyers Trust Account (IOLTA) Program exists in each state and the District of Columbia. In some states, the underlying authority for the program is a state statute; however, in most, it is by rule promulgated by the state's highest court. In Pennsylvania, the IOLTA Program was initially established by statute in 1989, but in 1996, the Supreme Court of Pennsylvania suspended the statute, assumed jurisdiction for the program in accordance with Pennsylvania's constitution, and made participation in the program mandatory by all licensed Pennsylvania lawyers.

The concept of the IOLTA program is simple. Clients and others frequently transfer money to lawyers to hold. When the amount is large or if the funds will be held for an extended period of time, lawyers invest them for the benefit of the client or third party. But, when the funds are small or expected to be held for a short time, they cannot practically be invested to benefit the owner. Pennsylvania Rule of Professional Conduct (RPC) 1.15 requires lawyers to maintain nominal and short term fiduciary funds in interest-bearing IOLTA accounts at financial institutions. Lawyers who infrequently handle fiduciary funds can request an exemption from the IOLTA requirements of the RPC. The lawyer's bank transfers the interest earned on IOLTA accounts to the IOLTA Board. Upon approval by the Supreme Court of Pennsylvania, the IOLTA Board distributes the IOLTA funds raised to non-profit organizations, law school administered clinical and externship programs, and administration of justice projects all of which provide civil legal services free of charge to poor and disadvantaged Pennsylvania residents.

Until the fiscal year ended June 30, 2003, the IOLTA Board's single major source of revenue had been the collection of interest earned on IOLTA accounts. Revenue generated by IOLTA accounts is dependent on the interest rate(s) credited by financial institutions on IOLTA accounts, service charges offset against the IOLTA interest, and the principal amount of funds maintained in the IOLTA accounts. Although IOLTA revenue can also be affected by the extent of lawyer compliance with the RPC, compliance is and has been nearly 100%.

Effective November 1, 2002, a second significant revenue source was established. A statute, Act 122 of 2002, a section of which is known as the Access to Justice Act (AJA), provides for the assessment and collection of a surcharge on all civil filings, as well as the recording of deeds and mortgages and their related filings, and criminal filings where a conviction or a guilty plea is obtained (see Note 5 to the financial statements). For the fiscal year ending June 30, 2005, \$7.5 million and for the fiscal year ending June 30, 2004, \$7.7 million of such charges were earmarked for the IOLTA Board's grants program targeted to civil legal services provided by non-profit legal aid organizations. The amount of the surcharge that is earmarked for the IOLTA Board is scheduled for legislative review before November 1, 2007 under a sunset provision of the statute.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

The IOLTA Board also receives some limited funding from voluntary lawyer contributions. Each year lawyers must renew their license to practice law in Pennsylvania, report information, and pay an annual assessment to the Disciplinary Board of the Supreme Court of Pennsylvania. Included in the mailing of the Annual Attorney Fee Form by the Disciplinary Board is an enclosure that requests a contribution that will be used to increase the organized pro bono representation of indigent Pennsylvania residents by lawyers in private practice. Pro bono representation is the provision of legal assistance by lawyers without the expectation of a fee for the services.

IOLTA BOARD'S ACTIVITY HIGHLIGHTS

National and other studies have concluded that only one of five indigent persons needing civil legal assistance actually receives the needed legal help. As a result, legal assistance is often rationed to those whose needs are determined the greatest, such as victims of domestic violence, tenants and homeowners facing the loss of housing, and families facing the loss of income.

All of the IOLTA Board's grants are directed to maintaining and increasing the access to and provision of civil legal assistance for Pennsylvania residents who need civil legal help, but who cannot afford to pay for the assistance of a lawyer. An additional objective of its grants to law schools and pro bono programs is to instill a public service, pro bono ethic in the law students and lawyer participants of the programs.

The IOLTA Board also seeks to increase the amount of revenue it has available for such grants. Finally, the IOLTA Board keeps track of lawyer compliance with the IOLTA requirements of RPC 1.15.

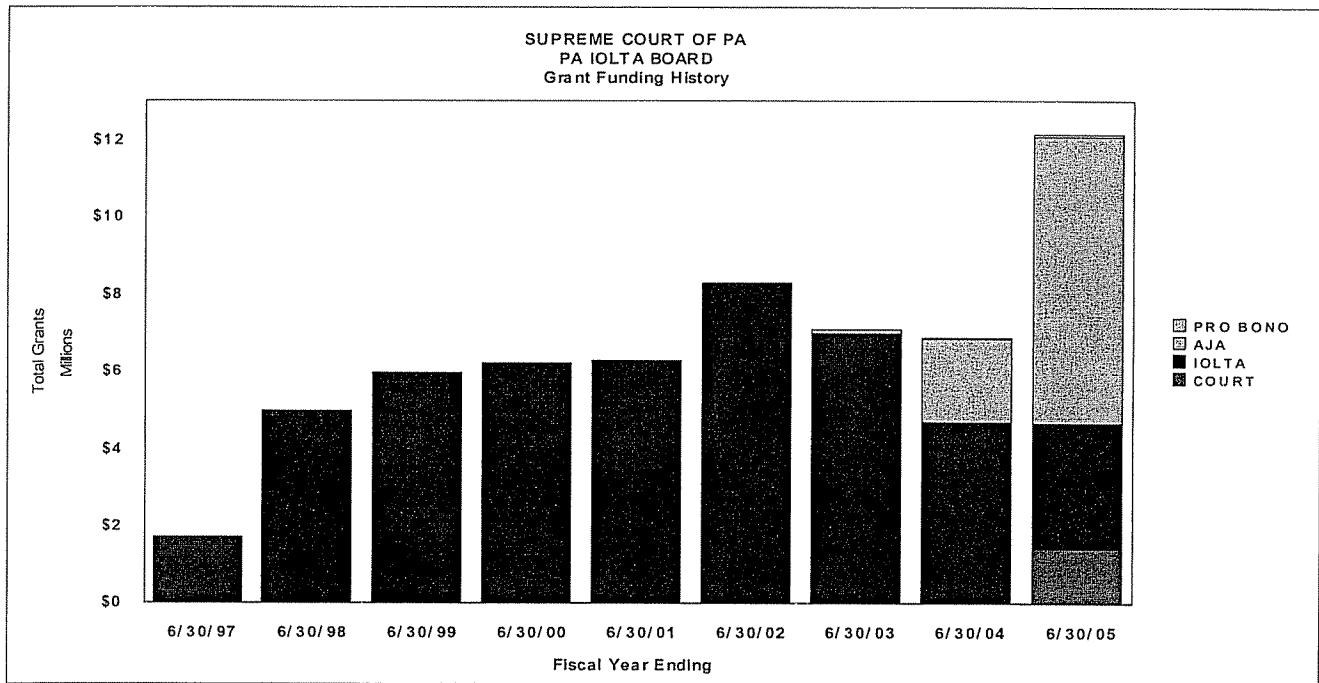
Overall Grant Activities

Since the inception of the IOLTA Board in Pennsylvania through June 30, 2005, about \$75.2 million of grants have been awarded (nearly \$59.6 of which were awarded while the IOLTA Board was under the jurisdiction of the Supreme Court - see graph on the following page). As can be observed from the graph displaying the grant funding history, while the IOLTA Board was under the jurisdiction of the Supreme Court, grants have generally increased over the years. However, a review of the graph also reveals that without the transfer of funds to the IOLTA Board by the Supreme Court, or the implementation of the AJA, the level of grants in recent years would be quite different. The transfer of funds by the Supreme Court was extraordinary and is not expected to occur again. Also, without legislative action, the AJA will sunset November 1, 2007.

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PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

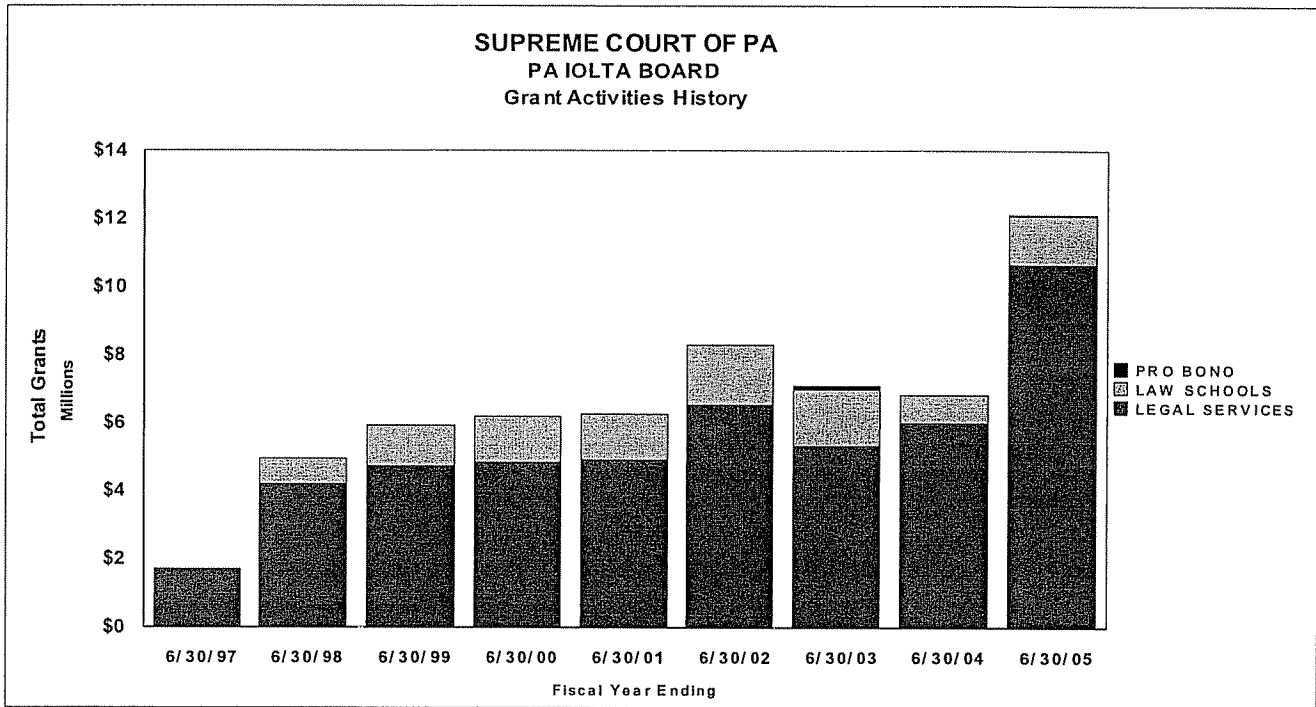


Since the IOLTA Board came under the jurisdiction of the Supreme Court of PA, most grants, \$49 million, have gone to legal services organizations, almost \$10.4 million to law school clinical and externship programs, and about \$170,000 to establish or expand county-based pro bono efforts. Until the enactment of the Access to Justice (AJA) statute, the grants were funded by IOLTA revenues and private attorney contributions.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED



With the infusion of new AJA funds last year and this year, grant awards to legal services organizations have increased. All of the AJA funding must be awarded to legal aid organizations. However, without the new AJA funding, grants to legal services organizations would have declined by 5.9% last year as compared to grant levels prior to the AJA.

Grant funds for law school clinics and internships had declined nearly 50% last year and were likely to continue declining because of historically low interest rates on IOLTA accounts. Law schools must plan their clinical and internship programs a year in advance to assure they can staff the clinics to accommodate student enrollment. The wide fluctuation of the IOLTA grants to the law schools last year and the likelihood of continued instability caused great planning difficulties for the law schools.

New funding from the AJA allowed legal services organizations dedicated funding through the Board; but without additional funding, the laws schools were realizing the full effects of the declining IOLTA revenues. Additionally, the IOLTA Board had to use nearly all of its cash reserves to fund its grants last year, and its cash position was very precarious.

Given these unusual and pressing circumstances, the Supreme Court of Pennsylvania authorized the one-time transfer of \$1.4 million from the Lawyers Fund for Client Security (LFCS) to the IOLTA Board. The LFCS is an unrelated organization that also operates under the jurisdiction of the Court. This one-time transfer allowed the Board to re-establish its cash position, award stabilizing grants to the law school clinics and internships this year without affecting the planned grants to legal services organizations.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

During this past year, the IOLTA Board, by policy, stabilized the annual grant levels to the law schools at \$200,000 each, or \$1.4 million annually. The IOLTA Board is considering cash balance policy changes which may finance stabilized grants to legal services organizations.

Revenue Enhancement

Two new revenue enhancement efforts were effective this year: the implementation of the Minor Judiciary Interest on Trust Account (MJ-IOTA) Program; and the establishment of the requirement that financial institutions pay interest rates on IOLTA accounts comparable to those of other depositors with similar balances.

The MJ-IOTA program is similar to the IOLTA program which covers certain attorney escrow accounts. Judicial officials maintain custodial accounts to hold the collection of fees and fines, collateral and cash bonds, restitution for victims of crime and other similar amounts, until the funds are ultimately transferred to the owners. Essentially, all of the funds handled by the minor judiciary are qualified funds, that is, funds which are nominal in amount or will be held for a short period of time. Effective February 1, 2005, judicial officials of the minor judiciary were required to establish an MJ-IOTA account for their custodial account. The MJ-IOTA accounts are treated the same as attorney IOLTA accounts by financial institutions. By June 30, 2005, all 554 of the affected judicial officials had taken action to have their MJ-IOTA account established. Gross interest on the accounts totaled approximately \$64,000. The accounts incurred nearly \$31,000 in service charges resulting in net interest of about \$33,000.

In April 2005, the Supreme Court of Pennsylvania amended RPC 1.15, which contains the underlying authority for the attorney IOLTA program. Included in the amended rule is the following requirement:

"The rate of interest payable on an IOLTA account shall not be less than the highest rate or dividend generally available from the financial institution to its non-IOLTA account customers when the IOLTA account meets or exceeds the same minimum balance and other account eligibility qualifications applicable to those other accounts."

This action is similar to that of other states and is the same as the requirement for the MJ-IOTA program. Representatives of the IOLTA Board and financial institutions will be meeting to further define the requirement. However, in response to requests for better yields on IOLTA and MJ-IOTA accounts, leading financial institutions have taken steps to pay comparable interest rates on the accounts immediately.

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PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

Attorney Compliance

Each year, the IOLTA Board notifies approximately 1,500 newly licensed Pennsylvania lawyers of their IOLTA responsibilities. Additionally, each year, the IOLTA Board compares fiduciary account information lawyers report to the Disciplinary Board of the Supreme Court of Pennsylvania attempting to locate IOLTA accounts established by lawyers at their financial institutions but which are not being reported to the IOLTA Board by the financial institutions. Contact is made with lawyers who report escrow accounts that should be established as IOLTA accounts, but which have not yet been so established by the lawyer.

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PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

COMMENTS ON FINANCIAL STATEMENTS

Condensed financial data extracted from the basic financial statements for the fiscal years ended June 30, 2005, 2004 and 2003 is as follows:

	2005	2004	2003
Capital assets	\$ 10,187	\$ 19,072	\$ 13,101
Other assets	11,859,158	10,617,406	3,991,210
Total assets	\$ 11,869,345	\$ 10,636,478	\$ 4,004,311
Total current liabilities	\$ 69,624	\$ 147,381	\$ 106,766
Invested in capital assets	10,187	19,072	13,101
Restricted net assets	11,649,953	10,362,921	3,824,872
Unrestricted net assets	139,581	107,104	59,572
Total net assets	11,799,721	10,489,097	3,897,545
Total liabilities and net assets	\$ 11,869,345	\$ 10,636,478	\$ 4,004,311
IOLTA interest, net of service charges	\$ 6,233,446	\$ 4,741,212	\$ 5,879,267
Access to Justice fees	7,488,907	7,659,679	2,942,829
Total operating revenues	13,722,353	12,400,891	8,822,096
Program administration	460,775	410,251	464,017
Grant awards			
Legal service organizations	10,676,994	6,006,015	5,356,000
Law schools	1,400,000	844,113	1,649,861
Pro bono grants	54,700	17,151	97,735
Total grant awards	12,131,694	6,867,279	7,103,596
Total operating expenses	12,592,469	7,277,530	7,567,613
Total non-operating revenues	180,740	1,468,191	54,546
Change in net assets	1,310,624	6,591,552	1,309,029
Net assets - July 1	10,489,097	3,897,545	2,588,516
Net assets - June 30	\$ 11,799,721	\$ 10,489,097	\$ 3,897,545

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PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

IOLTA Interest

As between the reported years, IOLTA interest has increased nearly \$1.5 million. Interest on IOLTA and MJ-IOTA accounts is dependent upon interest rates, service charges, principle balances, and attorney participation. Most of this increase is attributable to the higher interest rates which financial institutions have been paying (see *Revenue Enhancement*) in response to the request for comparable interest rates for IOLTA and MJ-IOTA accounts.

Legal Services Organization Grants

Grants to legal service organizations increased \$4.6 million or nearly 78%. This increase results from an increase in AJA revenues. The AJA is effective for five years, beginning November 1, 2002 and, absent legislative action, will sunset November 1, 2007. Proceeds from the AJA are available to the IOLTA Board for their statutory purposes in July of each year.

Grants totaling \$10,676,994 and \$6,006,015 were awarded in fiscal years ended June 30, 2005 and 2004 to thirty-four non-profit organizations that facilitate and/or provide civil legal assistance to the indigent and disadvantaged residents of Pennsylvania. The largest grant this past year, over \$8.9 million, was awarded to Pennsylvania Legal Services which is an administrative and support organization that oversees a statewide system of legal aid programs (the Pennsylvania Legal Aid Network) that is staffed by professional poverty law lawyers. That grant sought to provide general and specialized civil legal assistance to over 25,000 indigent persons in all sixty-seven counties in Pennsylvania.

Direct grants were made to some of the organizations of the Pennsylvania Legal Aid Network targeted to increase the access to civil legal help by assisting the organizations to implement and maintain region-wide telephone "help lines". Help lines make use of a toll-free number that callers from the area served by the program can use to seek legal assistance. After financial eligibility for service is determined, callers requiring direct representation are routed to the appropriate service office to schedule an appointment. Clients needing legal advice are immediately transferred to lawyers and paralegals staffing the telephone help line. Other grants were awarded to help remove barriers confronting individuals who were moving from public welfare to employment. Clients in such transition often need assistance with child care, health benefits, and transportation amongst other needs. Legal Aid programs were funded to help those individuals gain the assistance needed for a successful transition.

Grants were also awarded to civil legal service organizations that represent the disabled, victims of abuse, elderly, farm workers, institutionalized, or to provide specialized legal help for health, immigration, and other areas.

Law School Clinics and Internship Programs

Grants to law schools increased about \$556,000 or nearly 66%. The increase results from the transfer of funds by the Supreme Court of Pennsylvania which allowed the IOLTA Board to stabilize the annual level of grants for the law schools at \$1.4 million.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

MANAGEMENT'S DISCUSSION AND ANALYSIS UNAUDITED

Grants were awarded to each of the seven Pennsylvania law schools to help fund clinical programs that provide practical, supervised representational experiences for law students, as well as civil legal help for the indigent. The total IOLTA grant awards to the law schools were \$1,400,000 and \$844,113 in fiscal years ended June 30, 2005 and 2004. Each school received at least \$200,000 and \$111,930 in grant awards respectively. Fifteen clinics operated by the law schools received IOLTA grant support. The IOLTA grant for a clinic usually provided 30% to 60% of the direct cost of operating the clinic. At one law school, the IOLTA grant helped it initiate a farm workers' clinic, the first of its kind in the United States. At another school, the IOLTA funding helped it initiate an immigration law clinic. Externships at poverty law offices were also planned for students who would provide civil legal representation under the supervision of experienced poverty law practitioners.

Pro Bono Initiative

This year organized pro bono programs were funded in nine counties at the level of \$54,700. The grants were expected to help mobilize 354 lawyer volunteers to provide civil legal assistance for the indigent.

Non-Operating Revenue

Non-operating revenue decreased from the prior year by \$1.3 million. In the prior year, the IOLTA Board had received a transfer of funds authorized by the Supreme Court of Pennsylvania in the amount of \$1.4 million. Such a transfer was not repeated in the current year.

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

BALANCE SHEETS

JUNE 30, 2005 AND 2004

ASSETS

	<u>2005</u>	<u>2004</u>
Current assets		
Cash	\$ 2,739,822	\$ 1,721,716
Investments	10,693	-
Accounts receivable		
IOLTA interest	752,582	480,000
Access to Justice	8,343,644	8,365,064
Other	2,222	42,341
Prepaid expenses	10,195	8,285
Total current assets	<u>11,859,158</u>	<u>10,617,406</u>
Capital assets	96,482	119,422
Accumulated depreciation	<u>(86,295)</u>	<u>(100,350)</u>
	<u>10,187</u>	<u>19,072</u>
Total assets	<u>\$ 11,869,345</u>	<u>\$ 10,636,478</u>

LIABILITIES AND NET ASSETS

Current liabilities		
Accounts payable		
Legal service organizations	\$ 2,500	\$ 98,950
Law schools	-	7,665
Other	35,320	15,497
Accrued expenses	31,804	25,269
Total current liabilities	<u>69,624</u>	<u>147,381</u>
Net assets		
Invested in capital assets	10,187	19,072
Restricted to IOLTA program	3,216,851	1,991,246
Restricted to Access to Justice Program	8,433,102	8,371,675
Unrestricted	139,581	107,104
Total net assets	<u>11,799,721</u>	<u>10,489,097</u>
Total liabilities and net assets	<u>\$ 11,869,345</u>	<u>\$ 10,636,478</u>

The accompanying notes are an integral part of these financial statements.

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
Operating revenues		
IOLTA interest, net of service charges of \$262,184 and \$229,563	\$ 6,233,446	\$ 4,741,212
Access to Justice fees	7,488,907	7,659,679
Total operating revenues	13,722,353	12,400,891
Operating expenses		
Program administration	460,775	410,251
Grant awards		
Legal service organizations	10,676,994	6,006,015
Law schools	1,400,000	844,113
Pro bono grants	54,700	17,151
Total grant awards	12,131,694	6,867,279
Total operating expenses	12,592,469	7,277,530
Operating income	1,129,884	5,123,361
Non-operating revenues		
Contributions		
Pro Bono Initiative	87,177	64,683
Lawyer Fund for Client Security	-	1,400,000
Other interest and service charges, net	93,563	3,508
Total non-operating revenues	180,740	1,468,191
Change in net assets	1,310,624	6,591,552
Net assets - July 1	10,489,097	3,897,545
Net assets - June 30	\$ 11,799,721	\$ 10,489,097

The accompanying notes are an integral
part of these financial statements.

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

STATEMENTS OF CASH FLOWS

YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
Cash flows from operating activities		
IOLTA interest received	\$ 5,960,864	\$ 4,756,212
Access to Justice fees received	7,510,327	2,237,444
Other cash receipts	40,119	-
Cash paid to grant recipients	(12,235,809)	(6,826,024)
Cash paid to suppliers	(106,869)	(180,838)
Cash paid to employees	(305,264)	(207,758)
Other cash payments	(18,179)	(56,849)
	<u>845,189</u>	<u>(277,813)</u>
Net cash provided by (used in) operating activities		
Cash flows from non-capital financing activities		
Contributions:		
Pro Bono Initiative	87,177	64,683
Lawyer Fund for Client Security	-	1,400,000
	<u>87,177</u>	<u>1,464,683</u>
Net cash provided by non-capital financing activities		
Cash flows from capital and related financing activities		
Acquisition of capital assets	(2,822)	(13,914)
	<u>(2,822)</u>	<u>(13,914)</u>
Net cash used in capital and related financing activities		
Cash flows from investing activities		
Purchase of investments	(5,000)	-
Interest	93,562	3,508
	<u>88,562</u>	<u>3,508</u>
Net cash provided by investing activities		
Increase in cash	1,018,106	1,176,464
Cash - beginning	1,721,716	545,252
Cash - ending	<u>\$ 2,739,822</u>	<u>\$ 1,721,716</u>
Reconciliation of operating income to net cash provided by (used in) operating activities		
Operating income	\$ 1,129,884	\$ 5,123,361
Adjustments to reconcile operating income to net cash provided by (used in) operating activities		
Depreciation expense	11,707	7,943
Changes in assets and liabilities:		
Accounts receivable	(211,043)	(5,447,549)
Prepaid expenses	(1,910)	(2,183)
Accounts payable	(84,292)	30,573
Accrued expenses	843	10,042
	<u>845,189</u>	<u>(277,813)</u>
Net cash provided by (used in) operating activities		

The accompanying notes are an integral part of these financial statements.

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

On July 17, 1996, the Supreme Court of Pennsylvania amended Rule 1.15 of the Pennsylvania Rules of Professional Conduct which governs Pennsylvania attorneys' handling of fiduciary funds. The amendment requires that substantially all Pennsylvania attorneys place all fiduciary funds they handle in interest-bearing accounts and that the interest earned inure to the benefit of clients, qualifying third parties, or is given to the IOLTA program. Effective September 1, 1996, the Pennsylvania Interest on Lawyers Trust Account Board (the Board) was established to administer this program through a nine member Board, all of whom are appointed by the Supreme Court.

Reporting Entity

The Board's financial statements present the financial position and results of operations of the Board only. The Board does not exercise oversight responsibility for any other organization. It is a component unit of the judicial branch of the Commonwealth of Pennsylvania.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The financial statements of the Board are prepared in accordance with generally accepted accounting principles. The Board applies all relevant Governmental Accounting Standards Board (GASB) pronouncements and applicable Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless they conflict with GASB pronouncements. The Board does not apply FASB pronouncements issued after November 30, 1989.

The Board's financial statements report uses the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of the timing of related cash flows.

Restricted Resources

When both restricted and unrestricted resources are available for use, it is the Board's policy to use restricted resources first, then unrestricted resources as they are needed.

Estimates

The preparation of financial statements under the accrual basis of accounting requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

NOTES TO FINANCIAL STATEMENTS

Grants

The amendment to the Pennsylvania Rules of Professional Conduct requires that IOLTA interest be used for the following purposes; (1) delivery of civil legal assistance to the poor and disadvantaged in Pennsylvania by non-profit corporations described in Section 501(c)(3) of the Internal Revenue Code; (2) educational legal clinical programs and internships administered by law schools located in Pennsylvania; (3) administration and development of the IOLTA program in Pennsylvania; and (4) the administration of justice in Pennsylvania. Grants are generally awarded on an annual basis and grant payments are disbursed on a semi-annual or quarterly basis. Grants are expensed at the inception of the specified grant period.

Capital Assets

Capital assets consisting of furniture, equipment, computer software, and leasehold improvements are recorded at cost. Depreciation policies reflect the use of the straight-line method with useful lives of three and five years. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to income as incurred; significant renewals and betterments are capitalized. Deductions are made for retirements resulting from the renewals or betterments.

Net Assets

Net assets are classified in the following three components: invested in capital assets; restricted and unrestricted. Invested in capital assets consists of all capital assets, net of accumulated depreciation. Restricted consists of net assets for which constraints are placed thereon by regulations and enabling legislation, less any related liabilities. Unrestricted consists of the net assets of the Board, which are not restricted for any project or other purpose.

Risk Management

The Board is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Significant losses are covered by commercial insurance. There were no significant reductions in insurance coverage in fiscal year 2005. There were no significant claims in the current year or the two prior years.

Tax Status

The Board is exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Service Code and from Commonwealth of Pennsylvania corporate taxes.

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PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

NOTES TO FINANCIAL STATEMENTS

2. CASH AND CASH EQUIVALENTS AND INVESTMENTS

Under statute, the Board's deposits must be held in insured depositories. The Board may also invest in direct obligations of the U.S. Government and agencies thereof. The Board follows the policy of holding cash deposits in demand deposit and money market accounts of Pennsylvania financial institutions.

Custodial Credit Risk - Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Board's deposits may not be returned to it. As of June 30, 2005, \$2,349,119 of the Board's bank balances of \$2,449,119 was exposed to custodial credit risk as follows:

Uninsured and collateral held by pledging bank's trust department not in the Board's name	<u>\$ 2,349,119</u>
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As of June 30, 2004, \$1,636,404 of the Board's bank balances of \$1,736,404 was exposed to custodial credit risk as follows:

Uninsured and collateral held by pledging bank's trust department not in the Board's name	<u>\$ 1,636,404</u>
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(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

NOTES TO FINANCIAL STATEMENTS

3. CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2005 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets				
Furniture and equipment	\$ 76,070	\$ 2,822	\$ (22,018)	\$ 56,874
Software	39,153	-	(3,744)	35,409
Leasehold improvements	4,199	-	-	4,199
Total capital assets	<u>119,422</u>	<u>2,822</u>	<u>(25,762)</u>	<u>96,482</u>
Less accumulated depreciation for:				
Furniture and equipment	(57,221)	(10,644)	22,018	(45,847)
Software	(38,930)	(1,063)	3,744	(36,249)
Leasehold improvements	(4,199)	-	-	(4,199)
Total accumulated depreciation	<u>(100,350)</u>	<u>(11,707)</u>	<u>25,762</u>	<u>(86,295)</u>
Capital assets, net	<u>\$ 19,072</u>	<u>\$ (8,885)</u>	<u>\$ -</u>	<u>\$ 10,187</u>

Capital assets activity for the year ended June 30, 2004 was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets				
Furniture and equipment	\$ 64,351	\$ 11,719	\$ -	\$ 76,070
Software	36,959	2,194	-	39,153
Leasehold improvements	4,199	-	-	4,199
Total capital assets	<u>105,509</u>	<u>13,913</u>	<u>-</u>	<u>119,422</u>
Less accumulated depreciation for:				
Furniture and equipment	(51,611)	(5,610)	-	(57,221)
Software	(36,598)	(2,333)	-	(38,930)
Leasehold improvements	(4,199)	-	-	(4,199)
Total accumulated depreciation	<u>(92,408)</u>	<u>(7,943)</u>	<u>-</u>	<u>(100,350)</u>
Capital assets, net	<u>\$ 13,101</u>	<u>\$ 5,970</u>	<u>\$ -</u>	<u>\$ 19,072</u>

Depreciation expense for the years ended June 30, 2005 and 2004 was \$11,707 and \$7,943.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

NOTES TO FINANCIAL STATEMENTS

4. IOLTA REVENUES AND GRANT EXPENSES

Lawyers throughout Pennsylvania have established special interest-bearing IOLTA accounts with their local depository institutions for funds received by the lawyers in a fiduciary capacity which can not practically be invested to benefit the owner of the funds. The depository institutions transfer IOLTA interest earnings, net of service charges, to the Board. The Board uses these funds to make grants to not-for-profit corporations which operate in Pennsylvania, whose primary purpose is to provide civil legal services without charge to eligible clients. The Board can also provide grants to law schools in Pennsylvania for educational legal clinical programs and internships, and administration of justice. All of the Board's grants are directed to the provision of civil legal services for the poor and disadvantaged. Total grants awarded by the Board during the years ended June 30, 2005 and 2004, net of rescissions, amounted to \$12,131,694 and \$6,867,279.

During March 2005, the Board recommended, and the Supreme Court of Pennsylvania approved, \$12,281,931 in grants for the grant year July 1, 2005 through June 30, 2006.

5. ACCESS TO JUSTICE REVENUE AND GRANT EXPENSES

With the passage of Act 122 in 2002, an additional fee of \$10, starting November 1, 2002, was authorized to be charged and collected by prothonotaries, clerks of courts, clerks of orphans' courts, registers of wills, recorders of deeds, and the minor judiciary including district justices, Philadelphia Municipal Court, Philadelphia Traffic Court, and Pittsburgh Magistrates Court, on certain civil and criminal courthouse filings. In criminal matters the additional fee is collected if a conviction is obtained or a guilty plea is entered. Proceeds from the additional fees are transferred by the collecting authority to the Pennsylvania Department of Revenue for deposit into either the Judicial Computer System Augmentation Account (JCSAA) or the Access to Justice Account (AJA). The split of the collections between the two accounts is as follows:

<u>Fiscal Years Ending June 30:</u>	<u>JCSAA</u>	<u>AJA</u>
2003	90%	10%
2004	85%	15%
2005	85%	15%
2006, and thereafter	80%	20%

The AJA is scheduled to sunset on November 1, 2007. Funds in the AJA are distributed annually to the Pennsylvania Interest on Lawyers Trust Account Board for the provision of civil legal assistance for the Commonwealth's poor. The Board earned collections totaling \$7,488,907 and \$7,659,679 relating to the AJA during the years ended June 30, 2005 and 2004, of which \$6,984,500 and \$7,510,327 was available for appropriation for the 2005 and 2004 fiscal years.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

NOTES TO FINANCIAL STATEMENTS

During March 2005, the Board recommended, and the Supreme Court of Pennsylvania approved, \$7,342,644 in grants to Pennsylvania Legal Services for the grant period July 1, 2005 through June 30, 2006.

6. PRO BONO INITIATIVE CONTRIBUTIONS AND GRANT EXPENSES

In June 2001, the Chief Justice of the Supreme Court of Pennsylvania asked lawyers licensed to practice law in Pennsylvania to voluntarily contribute at least \$50 each to help fund the infrastructure necessary for organized county-based pro bono programs. The Board received contributions totaling \$87,177 and \$64,683 as a result of the appeal during the years ended June 30, 2005 and 2004. Grants to pro bono programs (included in amounts in note 4) by the Board totaled \$54,700 and \$17,151 during the years June 30, 2005 and 2004.

During March 2005, the Board recommended and the Supreme Court of Pennsylvania approved \$61,800 in Pro Bono grants for the grant period July 1, 2005 through June 30, 2006.

7. LAWYER FUND FOR CLIENT SECURITY

During the year ended June 30, 2004, the Supreme Court of Pennsylvania authorized a one-time transfer of \$1,400,000 to the Board from the Lawyer Fund for Client Security, a separate organization, also operated under the jurisdiction of the court. The intended use of the revenue was to fund law school grants for the fiscal year July 1, 2004 to June 30, 2005.

8. LEASES

The Board leases office space in Harrisburg under a three year operating lease. Lease expense for the years ended June 30, 2005 and 2004 amounted to \$21,400 and \$21,328. Minimum amounts payable under the lease of \$21,324 and \$17,770 are due for the years ending June 30, 2006 and 2007.

9. RETIREMENT PLAN

The Board sponsors a 403(b) retirement plan for employees. There were employer contributions of \$31,266 and \$29,441 to the plan for the year ended June 30, 2005 and 2004.

10. DEFERRED COMPENSATION PLAN

During the year ended June 30, 2004, the Board entered into a deferred compensation agreement with the Executive Director. The deferred compensation is to be paid to the Executive Director or his heirs in three substantially equal annual installments an amount equal to the fair market value of the assets in the Rabbi Trust as of that date. The Board accrued \$10,200 for the agreement as of June 30, 2005.

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

NOTES TO FINANCIAL STATEMENTS

9. RETIREMENT PLAN

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SUPPLEMENTARY INFORMATION

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

DETAILED SCHEDULE OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

YEAR ENDED JUNE 30, 2005
(WITH COMPARATIVE TOTALS FOR 2004)

	General	Access to Justice	Pro Bono Initiative	Property	Total 2005	Total 2004
Operating revenues						
IOLTA interest, net of service charges of \$262,184 and \$229,563	\$ 6,233,446	\$ -	\$ -	\$ -	\$ 6,233,446	\$ 4,741,212
Access to Justice fees	-	7,488,907	-	-	7,488,907	7,659,679
Total operating revenues	<u>6,233,446</u>	<u>7,488,907</u>	<u>-</u>	<u>-</u>	<u>13,722,353</u>	<u>12,400,891</u>
Operating expenses						
Program administration	349,054	100,014	-	11,707	460,775	410,251
Grant awards						
Legal service organizations	3,282,167	7,394,827	-	-	10,676,994	6,006,015
Law schools	1,400,000	-	-	-	1,400,000	844,113
Pro bono grants	-	-	54,700	-	54,700	17,151
Total grant awards	<u>4,682,167</u>	<u>7,394,827</u>	<u>54,700</u>	<u>-</u>	<u>12,131,694</u>	<u>6,867,279</u>
Total operating expenses	<u>5,031,221</u>	<u>7,494,841</u>	<u>54,700</u>	<u>11,707</u>	<u>12,592,469</u>	<u>7,277,530</u>
Operating income (loss)	<u>1,202,225</u>	<u>(5,934)</u>	<u>(54,700)</u>	<u>(11,707)</u>	<u>1,129,884</u>	<u>5,123,361</u>
Non-operating revenues						
Contributions						
Pro Bono Initiative	-	-	87,177	-	87,177	64,683
Lawyer Fund for Client Security	-	-	-	-	-	1,400,000
Other interest and service charges, net	25,638	67,925	-	-	93,563	3,508
Total non-operating revenues	<u>25,638</u>	<u>67,925</u>	<u>87,177</u>	<u>-</u>	<u>180,740</u>	<u>1,468,191</u>
Change in net assets	1,227,863	61,991	32,477	(11,707)	1,310,624	6,591,552
Reclassification of net assets						
Acquisition of property	(2,258)	(564)	-	2,822	-	-
Net assets - July 1	<u>1,991,246</u>	<u>8,371,675</u>	<u>107,104</u>	<u>19,072</u>	<u>10,489,097</u>	<u>3,897,545</u>
Net assets - June 30	<u>\$ 3,216,851</u>	<u>\$ 8,433,102</u>	<u>\$ 139,581</u>	<u>\$ 10,187</u>	<u>\$ 11,799,721</u>	<u>\$ 10,489,097</u>

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

SCHEDULE OF PROGRAM ADMINISTRATION EXPENSES AND PROPERTY ACQUISITIONS - BUDGET AND ACTUAL

YEAR ENDED JUNE 30, 2005

	<u>Budget (Unaudited)</u>	<u>General</u>	<u>Access to Justice</u>	<u>Property</u>
Program administration expenses				
Personnel				
Wages	\$ 225,528	\$ 158,073	\$ 59,413	\$ -
Fringe benefits	83,072	70,394	17,628	-
Total personnel	<u>308,600</u>	<u>228,467</u>	<u>77,041</u>	<u>-</u>
Operating				
Consultants and contract services	47,000	52,866	6,045	-
Office supplies	9,000	7,611	1,902	-
Postage	3,000	2,368	592	-
Printing and publications	16,000	7,710	1,927	-
Rent	21,400	17,120	4,280	-
Telephone	6,000	3,947	987	-
Temporary help	600	479	120	-
Travel - staff and board	16,000	13,861	3,465	-
Depreciation	12,000	-	-	11,707
Insurance	7,600	5,749	1,437	-
Equipment maintenance	21,000	8,193	2,048	-
Other	2,800	683	170	-
Total operations	<u>162,400</u>	<u>120,587</u>	<u>22,973</u>	<u>11,707</u>
Total program administration expenses	<u>\$ 471,000</u>	<u>\$ 349,054</u>	<u>\$ 100,014</u>	<u>\$ 11,707</u>
Property acquisitions				
Equipment and software purchased	<u>\$ 54,000</u>	<u>\$ 2,258</u>	<u>\$ 564</u>	<u>\$ -</u>

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

SCHEDULES OF GRANT RECIPIENTS

YEARS ENDED JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>2004</u>
Legal service organizations		
Aids Law Project	\$ 25,000	\$ 15,500
Allegheny County Bar Foundation	50,000	40,000
Allegheny County CASA Program	40,000	20,000
Community Impact Services	15,000	-
Community Legal Services	51,804	35,000
Consumer Bankruptcy Assistance Project	25,000	22,000
Disabilities Law Project	30,000	20,000
Education Law Center	30,000	20,000
Friends of Farmworkers	260,000	170,000
HIAS & Council Migration Services of Philadelphia	61,000	15,000
Homeless Advocacy Project	17,000	12,000
Juvenile Law Project	30,000	20,000
Lackawanna Pro Bono, Inc.	20,000	15,000
Legal Aid of Southeastern PA	94,517	70,400
Legal Aid Society of Pittsburgh/Kids Voice	65,000	35,000
Legal Clinic for the Disabled	21,000	19,000
Southwestern PA Legal Services	108,579	60,000
Lewisburg Prison Project	50,000	26,600
MidPenn Legal Services	90,000	45,000
North Penn Legal Services	204,861	50,400
Northwestern Legal Services	39,650	27,700
PA Health Law Project	65,000	38,000
PA Immigration Resource Center	40,000	25,000
Pennsylvania Legal Services	8,910,583	5,010,915
Philadelphia Legal Assistance	15,000	8,500
Philadelphia Volunteer Lawyers for the Arts	12,000	7,000
Philadelphia Volunteers for the Indigent Program	60,000	45,000
Protection from Abuse Coordinated Services, Inc.	30,000	20,000
Public Interest Law Center of Philadelphia	25,000	18,000
Regional Housing Legal Services	12,000	12,000
Senior Law Center	85,000	18,000
Support Center Child Advocates	41,000	35,000
Westmoreland Bar Foundation	32,000	20,000
Women Against Abuse Legal Center	21,000	10,000
	<hr/>	<hr/>
Total legal service organizations	10,676,994	6,006,015

(continued)

PENNSYLVANIA INTEREST ON LAWYERS TRUST ACCOUNT BOARD

SCHEDULES OF GRANT RECIPIENTS (Cont'd)

YEARS ENDED JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>2004</u>
Law schools		
Pennsylvania State University -		
Dickinson School of Law	200,000	172,506
Duquesne University	200,000	111,930
Temple University	200,000	111,930
University of Pennsylvania	200,000	111,930
University of Pittsburgh	200,000	111,930
Villanova University	200,000	111,930
Widener University	200,000	111,957
	<u>1,400,000</u>	<u>844,113</u>
Total law schools		
Pro bono grants		
Bedford County Bar Association	-	(9,000)
Chester County Bar Association	7,000	-
Lackawanna Pro Bono, Inc.	5,000	4,500
Laurel Legal Services (Cambria County)	10,000	-
Legal Aid of Luzerne County	-	10,651
Middle District Bankruptcy Court	5,000	-
MidPenn Legal Services	15,000	-
Neighborhood Legal Services (Butler County)	5,000	-
Northampton Bar Association	2,700	-
Warren Bar Association	-	6,000
Wyoming Bar Association	5,000	5,000
	<u>54,700</u>	<u>17,151</u>
Total pro bono grants		
Total grant awards	<u>\$ 12,131,694</u>	<u>\$ 6,867,279</u>