LCRO 126/2012

CONCERNING	an application for review pursuant to section 193 of the Lawyers and Conveyancers Act 2006
AND	
CONCERNING	a determination of [North Island] Standards Committee
BETWEEN	**MS VX and VXZ** Applicant
AND	**[NORTH ISLAND] STANDARDS COMMITTEE** Respondent

The names and identifying details of the parties in this decision have been changed.

DECISION

Introduction

[1] This is an application for review of a determination by the Standards Committee in which it found that VXZ, the law firm operated by Ms VX, had breached the provisions of s 110(2) of the Lawyers and Conveyancers Act 2006 (the Act) and issued a wrongful certificate under s 112(2) of the Act.

[2] This decision is of some importance in that it concerns an arrangement between VXZ and the law firm WAA whereby VXZ operated without a trust account (and certified accordingly to the New Zealand Law Society) and directed funds paid to VXZ clients pursuant to Employment Relations Act proceedings into WAA's trust account.

Background

[3] Following an inspection by the New Zealand Law Society Inspectorate of WAA's trust account, the Standards Committee commenced an own motion investigation pursuant to s 130(c) of the Act.

[4] Mrs AT, an NZLS audit inspector, was appointed pursuant to s 144 of the Act to conduct an investigation and reported to the Committee on 15 February 2011. In her report, Mrs AT advised:

> two hundred and fifty three sub ledgers have been opened in the name of [VXZ] within the trust account maintained by [WAA].
>
> ...
>
> I have spoken with Ms [VX] who explained that she would not be able to state "hand on heart" that she had obtained a letter of engagement from each and every client although it was her normal policy to do so.

[5] VXZ standard terms of engagement included the following paragraph:

> [VXZ] does not operate a Solicitor's Trust Account but has an arrangement with [WAA] Barristers & Solicitors to use their Trust Account. By authorising [Ms VX] and/or [VXZ] to act on your behalf, you are also authorising any monies to be collected or held on your behalf, to be depotised into the [WAA] Barristers & Solicitors Trust Account to be dealt with in accordance with your instructions, and the rules and legislation that govern Solicitor's Trust Accounts.

[6] Mrs AT's report continued:[1]

> I understand that Ms [VX] deals only with employment relationship matters and she stated that authorities to lodge the monies within the [WAA] trust account were contained in her clients' settlement statements. However I have found that other monies had been transferred from a bank account in the name of [VXZ] to cover disbursements and fees payable to [WAA].
>
> [Mr WB] of [WAA] explained that the bank account in the name of [VXZ] was operated jointly by Ms [VX] and the partners of [WAA] and if fees were not to be taken from settlement funds clients were requested to pay monies to cover their legal costs into this account.
>
> ...
>
> From my enquiry into the administration of the account by [WAA], I found that Ms [VX] rendered each client an individual bill of costs and these were handed to the trust account administrator at [WAA] to enable disbursements to be debited to the ledger together with 50% of the costs payable to [WAA].

[1] Report from Mrs AT to NZLS, 15 February 2011 at p 2.

If compensation monies had been received on behalf of the clients, it was the normal practice to debit disbursements and 50% of the fees to the [WAA] float account and to pay the remaining share of the fees to the [VXZ] business account by direct credit.

However, if the fees were to be paid from monies received into the joint business account a pro-forma bill to cover the [WAA] costs was posted to the trust ledger and Ms [VX] was responsible for drawing her share of the fees from that account.

It was not [WAA] policy to render a bill of costs to [VXZ].

[7] By way of further explanation it is helpful to refer to the following extracts from a letter dated 28 October 2010 sent by Mr VZ, counsel engaged by Ms VX, to the Standards Committee:

1. [VXZ] is a company of which [Ms VX] is the Director.

2. The company occupies office space in the premises of the law firm [WAA]. It also has use of the firm's reception, accounting, power and telephone facilities.

3. Instead of paying rent as a sub-tenant, the company pays for its use of the facilities by dividing its fee income equally between [WAA] and itself.

4. The legal practice of [VXZ] is that of representation of claims by present and former employees, employers and unions made under the Employment Relations Act 2000.

5. Ms [VX] has the option of carrying out such services as a Barrister and Solicitor (which she has chosen), a Barrister or as a non-lawyer advocate. Her view is that she prefers to practise as a lawyer, thus excluding the advocate option. She believes that as a Barrister and Solicitor she can function professionally in a more straightforward and efficient way than as a Barrister. Likewise from [WAA's] perspective that also is preferred.

6. Payments for claims made under the Employment Relations Act 2000 are required by the Act to be made either to the claimant directly by the payer or into a Solicitor's trust account. I attach a copy of s l50A with commentary and of ss149(3) and 150(3) which are referred to in s150A. Thus [VXZ] arranges for its clients to pay into the [WAA's] trust account. Also enclosed is a copy of a settlement form commonly in use for the purpose of the Act.

7. In the Inspectorate's report of 31 May 2010 to [WAA], reference was made to there having been 193 matters for which ledgers had been set up. This number needs to be put into perspective. It is made up of three categories: clients of

> [WAA] referred to [VXZ] who remain [WAA's] clients; clients of [VXZ] for whom compensation monies are received; and clients for whom no compensation is received and only fees are transacted. The middle group is the only one relevant for the present purpose and at a maximum would comprise a third of total matters.

[8] The settlement form referred to by Mr VZ in paragraph 6 included the following direction by the client:

> Within seven days of both parties signing this record of settlement the employee shall receive:
>
> i. A certificate of service outlining his years of service, roles and duties; and
>
> ii. $ [AMOUNT] in accordance with section 123(1)(c)(1) of the Employment Relations Act 2000 to be made by direct credit into the [WAA] Barrister & Solicitors Trust Account [bank account number].

[9] The above paragraphs from Mrs AT's report and Mr VZ's letter record the nature of the arrangement between VXZ and [WAA].

The Standards Committee determination

[10] Having considered all of the material before it, which included submissions from Mr VZ and advice from Mr AS, the Standards Committee recorded its determination in the following way:[2]

> 17. Having inquired into the matter and conducted a hearing the Committee determined that there had been unsatisfactory conduct on the part of Ms [VX] pursuant to s152(2)(b)(i) and on the part of [VXZ] pursuant to s152(2)(b)(ii) on the basis of:
>
> a. Breach of s 110(2) of the Act; and
>
> b. Issuing a wrongful certificate under s 112(2).
>
> 18. The Committee referred to s 17(2), by which a lawyer who is a director or shareholder of an incorporated firm is subject to all the professional obligations applicable to a lawyer practising on his or her own account.

[11] It made the following Orders:

> a. That Ms [VX] be censured pursuant to s 156(1)(b) of the Act;

[2] [North Island] Standards Committee determination, 3 May 2012.

b. That Ms [VX] and [VXZ] jointly and severally pay to the New Zealand Law Society by 3 June 2012 a fine of $1,000 pursuant to s 156(1)(i) of the Act;

c. That Ms [VX] and [VXZ] jointly and severally pay to the New Zealand Law Society by 3 June 2012 the sum of $2,000 in respect of the costs and expenses of and incidental to the inquiry and the hearing pursuant to s 156(i)(n) of the Act;

d. That the name of the practitioner not be published.

[12] VXZ have applied for a review of that determination.

Review

[13] This review proceeded by way of a hearing in Hamilton held on 26 March 2013. VXZ were represented by Mr VZ and the Standards Committee was represented by Mr AS, accompanied by Mrs AT. Messrs WA and WB also attended the hearing as the review was conducted in conjunction with the review of a determination by the Standards Committee concerning their conduct in relation to another matter.

[14] An initial observation to be made is that it is somewhat disappointing that this matter has proceeded by way of an investigation followed by findings against the practitioners. I note that Mr WB sought to meet with the Complaints Service for the purpose of resolving the matter by conciliation, negotiation or mediation in terms of s 143 of the Act but it does not appear that any such meeting occurred.

[15] I understood Mr AS to submit that once the Standards Committee became appraised of the matter by way of an own motion investigation, it was required to continue through to a determination. The Standards Committee has a discretion to determine at any time to take no further action in respect of a complaint or matter,[3] so I do not necessarily agree with that comment (if I have understood Mr AS correctly); but in any event, it does not seem that any of the lawyers involved accepted the possibility that the arrangement did not comply with provisions of the Act nor indicated a willingness to change the procedures that they had established.

Has there been a breach of s 110(2) of the Lawyers and Conveyancers Act 2006?

[16] Mr AS submitted that the arrangement between VXZ and [WAA] breached the policy of the Act and the specific requirements of s 110(2). In broad terms, he submitted that it would be undesirable for lawyers who are exempt from the requirements of the Lawyers and Conveyancers Act and the Trust Account

[3] Section 152(2)(c) Lawyers and Conveyancers Act 2006.

Regulations[4] by reason of the fact that they do not operate a trust account, to conduct significant trust account activity through what he referred to as a "surrogate" trust account.

[17] The validity of that submission is self evident. The Act and the Regulations are designed to ensure protection of client funds, and if a lawyer is able to avoid the application of the various provisions by an arrangement such as this, that objective would not be met.

[18] In addition, Mr AS argued that the arrangement adopted by the lawyers confused the identity of the lawyer receiving the money with that of the lawyer (or law firm) which held the money. The principle that the lawyer receiving the money should be the same lawyer who holds the money also meets with ready acceptance.

[19] Section 110(2) of the Act provides as follows:

> (2) An incorporated firm that, in the course of its practice, receives money for, or on behalf of, any person-
>
> > (a) must ensure that the money is paid promptly into a bank in New Zealand to a general or separate trust account of the firm; and
> >
> > (b) must hold the money, or ensure that the money is held, exclusively for that person, to be paid to that person or as that person directs.

[20] The issue for determination involves a consideration of whether or not VXZ was in receipt of client funds. Section 110(3) of the Act provides a deeming provision in this regard:

> (3) For the purposes of this section, a practitioner or an incorporated firm is deemed to have received money belonging to another person if-
>
> > (a) that person, or a bank or other agency acting for, or on behalf of, that person, deposits funds by means of a telegraphic or electronic transfer of funds into the bank account of-
> >
> > > (i) the practitioner or incorporated firm; or
> > >
> > > (ii) a person who, or body that, is, in relation to the practitioner, a related person or entity; or

[4] Lawyers and Conveyancers Act (Trust Account) Regulations 2008.

> (b) the practitioner or incorporated firm takes control of money belonging to that person.

[21] Mr VZ submitted:[5]

- The single issue turns on whether VXZ had received monies for clients thereby triggering s 110.
- It follows that the process followed by VXZ was important.
- VXZ provided standard terms of engagement which explained that the firm did not have a trust account but instead had an arrangement with WAA to use its trust account.
- The client, by having VXZ acting for him or her, was authorising any money obtained to be deposited with WAA.
- Those funds would be dealt with in accordance with the client's instructions and the law governing solicitors' trust accounts. The form also authorised deduction of invoiced costs from the trust account.
- Any settlement in terms of the Employment Relations Act 2000 was recorded by an agreement in which the client directed that funds be paid to WAA's trust account.
- In no case did VXZ receive money for a client from a settlement and therefore neither VXZ nor Ms VX ever actually received settlement money for the purposes of s 110.
- Mr VZ disagreed with the Committee when it appeared to "have considered that the term "receives money for..." involves the concept of control, and therefore if [VXZ] had control, it is deemed to have received money."[6]
- He further disagreed that VXZ ever had control of any money and that s 110(3)(b) did not apply. He submitted that:[7]

> There was a clear documented path for settlement monies to follow: the terms of engagement Letter, the Employment Relations Act (to a solicitor) and the Settlement Agreement, followed by the direct credit or cheque to [WAA]. Ms [VX] was unable to have a role, or intervene, in that process. To

[5] Submissions from Mr VZ to LCRO, 25 March 2013.
[6] Above n 5 at [9].

> do so would have been in breach of [VXZ's] own terms of engagement letter, or for that matter s 150A [of the Employment Relations Act 2000].

- Mr VZ submits that for a lawyer to have control he or she:[8]

> has to have stepped in, or at least been put in that position by the client, in which she/it is then able to carry out the s 110 obligations. The "control" has to be of that kind for the provision to have no meaning in the context of the section.

He argues that "the control has to equate with actual receipt in terms of what the Practitioner can do about the funds."[9]

- Mr VZ compared the provisions of s 110(3)(a) (which requires the Practitioner to have the ability to directly use the funds) with those of s 110(3)(b).

[22] For the Standards Committee Mr AS submitted at the review hearing:

- The interpretation of the trust account provisions must be approached from the perspective of the client and a technical interpretation of the provisions that serves the lawyers can only stand scrutiny if they serve and reinforce the protective purposes of a lawyer's trust account.

- VXZ terms of engagement referred to instructions provided to "us" i.e. VXZ.

- The terms of engagement refer to funds being paid to WAA trust account to be held "in accordance with your instructions" which Mr AS interprets as being instructions to VXZ.

- The funds were held by WAA for the credit of VXZ. In the event of a dispute as to that firm's fees, Mr AS asked whose instructions WAA would act on - VXZ seeking payment of fees, or the client to whom the funds belonged?

- Whether or not the funds were received by VXZ or directly into WAA's trust account, VXZ had control of the funds for all meaningful purposes.

- Clients would have understood that any instructions with regard to the funds were required to be directed to VXZ.

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[7] Above n 5 at [10].
[8] Above n 5 at [11].
[9] Above n 8.

[23] The single issue to determine is whether or not VXZ received, or took control of, client funds.

[24] By virtue of the direction given by the firm's clients (that any payments made were to be directed to WAA's trust account) the firm did not actually at any time "receive" funds from its clients. They were diverted to WAA.

[25] The question therefore becomes whether or not VXZ took control of those funds.[10]

[26] It is pertinent at this stage to recall that the client recorded in WAA's trust account was VXZ. A reference to the ledgers provided in the course of the own motion investigation show that the client is recorded as "VXZ re [name of client]".

[27] Regulation 12(6)(b) of the Trust Accounts Regulations provides:

> A practitioner may make transfers or payments from a client's trust money only if-
>
> (a) the client's ledger account has sufficient funds and they are available for that purpose; and
>
> (b) the practice obtains the client's instruction or authority for the transfer or payment, and retains that instruction or authority (if in writing) or a written record of it ... (the remainder of the regulation is not relevant to this matter).

[28] Consequently, no payment out of the account could be made without the authority of VXZ.[11] Although separate ledger accounts were created for each person within that client account, that did not alter the fact that the client was recorded as VXZ.

[29] Stripping away all the assurances provided by Messrs WB and WA, the simple fact of the matter is that the trust account clearly recorded VXZ as the client. The client was not recorded as the individual for whom VXZ was acting. If they were, they would have been recorded in the same way as WAA's own clients who were referred to VXZ.

[30] It would be expected that the lawyers would have carefully considered the arrangement before it was put in place and that Messrs WB and WA would have been conversant with the basis on which the arrangement was established. It is therefore difficult to ignore the initial responses from Mr WB to Mrs AT and the Lawyers Complaints Service and I have some doubt about the statements made by Messrs WA

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[10] Section 110(3)(b) Lawyers and Conveyancers Act 2006.
[11] Regulation 6(b) Lawyers and Conveyancers Act (Trust Account) Regulations 2006.

and WB that they always considered they held the funds to the order of the individual client.

[31] Mr WB responded to Mrs AT's initial report dated 7 July 2010:

> We have opened a ledger in the name of [VXZ] ("the company"). That ledger is under the control of [Ms VX], who operates as a solicitor on her own account under the name or style of [VXZ], sub-leasing accommodation at our premises.

[32] In the same letter, Mr WB wrote, "[w]e hold the money exclusively for the Company [VXZ] and this is paid as the Company directs."[12]

[33] Some months later (on 4 March 2011) Mr WB again wrote to the Standards Committee:

> We ([WAA]), in the course of our practice, received money for or on behalf of [VXZ] and we ensured that the money was paid promptly into a bank account in New Zealand to a separate trust account in the name of [WAA] and we held that money exclusively for [VXZ] to be paid to [VXZ] as it directed.

[34] There can be no clearer statements than those.

[35] Mr WB however then qualifies those statements by advising that they were aware of a "sub-trust" and that VXZ had obligations to "its particular clients".[13] The implication here would appear to be that WAA were assuming the obligations of VXZ to its clients in respect of the funds. That is a concept which does not sit comfortably with a lawyer's direct obligations to his or her clients.

[36] The affidavit from Mr WD (the firm's accountant) provided in the course of this review, only serves to further underline the reality that in terms of the Act and the Trust Account Regulations, the funds were under the control of VXZ. I refer to paragraph 5 of Mr WD's affidavit:[14]

> On instructions from [Mr WA] and [Mr WB], the partners of [WAA], I established within the trust account of [WAA] a client account for [Ms VX] under the name of "[VXZ]" which was Ms [VX]'s trading name.

[37] At paragraph 7.3 of that affidavit Mr WD goes on to depose that "[i]n the case of [Ms VX] the "Cheque Authority" form would be filled out either by her or by her

[12] Letter from Mr WB to NZLS, 7 July 2010.
[13] Letter from Mr WB to NZLS, 4 March 2011.
[14] Affidavit of Mr WD, 15 March 2013 at [5].

secretary and given to our Accounts Clerk."[15]

[38] These statements reinforce the reality that the funds were under the control of VXZ regardless of the actions taken by Messrs WA and WB. They acted on requests from Ms VX.

[39] I also anticipate that Ms VX would have wanted to make sure that payment of her fees was secure. If the funds were to be held to the order of her clients then this could not have been guaranteed. If WAA were to operate on her instructions, then payment was secure.

[40] By letter dated 28 October 2010, Mr VZ expressed the structure somewhat differently. In that letter he stated:[16]

> The monies in the sub-ledgers are not under the control of [VXZ]. [WAA] alone have the ability to pay money out by trust account cheques or direct debit to the client or at the client's directions. Ms [VX] can and does make a request of [WAA] to pay monies out, but she has no ability to perform that function. The decision-making and implementation is [WAA's] alone.

[41] This however somewhat begs the question as to whose instructions WAA were bound to act upon in terms of the Act and the Regulations. It highlights the confusion that Mr AS refers to.

[42] In his submissions, Mr VZ argued that Mr WB had been imprecise in his use of terminology and that his statements did not reflect the actual position. It is imperative that any dealings with client funds are straight forward and clear. The client must know without doubt that his or her funds are at all times held strictly to his or her order. Conversely, the lawyer must acknowledge without question, the right of the client whose funds they are holding to direct how those funds are to be applied. Where client funds are concerned, there can be no room for imprecise terminology or misunderstandings. These requirements are not met by the arrangement between VXZ and WAA.

[43] I therefore find that the funds were in reality under the control of VXZ. That company was recorded as the client in WAA's trust account and the partners of WAA were obliged to follow Ms VX's directions notwithstanding their statements to the contrary. It therefore follows that VXZ is in breach of s 110(2) of the Act as the funds were not paid into a trust account operated by that firm.

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[15] Above n 14 at [7.3].

[44] As a result of this finding, it follows also that Ms VX gave a false certificate in terms of s 112(2) of the Act.

[45] The Standards Committee has noted in its decision that s 17(2) of the Act provides that a lawyer who is a director or share holder of an incorporated firm is subject to all the professional obligations applicable to a lawyer practicing on his or her own account. It therefore follows that the findings against VXZ are also made against Ms VX.

Standards Committee Orders

[46] The Standards Committee imposed a fine of $1,000 and ordered Ms VX and VXZ to pay the sum of $2,000 by way of costs. The function of a penalty in a professional context is to punish the practitioner, to act as a deterrent to other practitioners and to reflect the public's and the profession's condemnation of the practitioner.[17] Weighed against these criteria, I see no reason to interfere with these Orders.

[47] I have also given separate consideration as to whether or not the censure imposed by the Standards Committee is appropriate.

[48] When viewing the correspondence between Ms VX and the Lawyers Complaints Service, it is apparent that Ms VX did not accept Mrs AT's criticism of the arrangement, and her responses were somewhat less than cooperative. This response contrasts with the responses of [name] and [name] in the case involving similar facts which I understand received some publicity in [North Island]. In that case, both lawyers readily acknowledged that the arrangement did not comply with the Act (the Law Practitioners Act 1982 in that case) and ceased the arrangement immediately.

[49] In addition the arrangement was clearly designed to allow VXZ to operate without a trust account but at the same time the firm was required by the Employment Relations Act to have any funds awarded to clients paid into a solicitors' trust account. Instead of adopting the simple response of establishing its own trust account, the firm chose to establish an arrangement with WAA to avoid the obligations that are imposed on law firms which operate a trust account. This indicates an unwillingness to meet the obligations imposed on a lawyer who wishes to receive client funds, and to this end I consider that a censure was warranted.

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[16] Letter from Mr VZ to NZLS, 28 October 2011 at [14].
[17] *Wislang v* M*edical Council of New Zealand* [2002] NZAR 573.

Decision

Pursuant to s 211(1)(a) of the Lawyers and Conveyancers Act 2006, the determination of the Standards Committee is confirmed.

Costs

In accordance with the Costs Orders Guidelines issued by this Office, costs orders follow where an adverse finding is made or upheld against a practitioner. Pursuant to s 210(1) of the Lawyers and Conveyancers Act, VXZ and Ms VX (jointly and severally) are to pay the sum of $1,200 to the New Zealand Law Society by way of costs, such sum to be paid by no later than 5 July 2013.

DATED this 5th day of June 2013

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O W J Vaughan
Legal Complaints Review Officer

In accordance with s.213 of the Lawyers and Conveyancers Act 2006 copies of this decision are to be provided to:

Ms VX as the Applicant
Mr VZ as the Representative for the Applicant
The [North Island] Standards Committee as the Respondent
Mr AS as the Representative for the Respondent
The New Zealand Law Society