LCRO 226/2011

CONCERNING	An application for review pursuant to section 193 of the Lawyers and Conveyancers Act 2006
AND	
CONCERNING	a determination of the Otago Standards Committee
BETWEEN	**TW** Applicant
AND	**NH** Respondent

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

DECISION

Background

[1] NH complained about the conduct of TW when he acted as solicitor for the estate of NG (NH's aunt). NG had died in December 2008, leaving a life interest in a third of her estate to NH's father, NF. The capital was to be paid to NH on the death of NF.

[2] At the centre of this complaint is the fact that TW advanced, without authority, $250,000.00 of the capital to NF by way of an unsecured loan in October 2010.

[3] When NH later learned about his entitlement he was unhappy with the fact that the advance had been made in a way which meant his interest was not secured. It transpired that NF used a large part of the advance and was not in a position to repay the loan to the estate. Ultimately it was agreed that the interests of the respective parties would be valued according to actuarial tables and distributed (to avoid the need to further administer the interest).

[4] It appears that the value of the portion of the estate held to the account of NF (including the debt owed by NF to the estate in respect of the advance), when the settlement between NF and NH was reached, was $327,685.41. Of that sum TW noted that $6267.41 was income accrued since the date of death of the testatrix (being 1/3 of the income on the assets of the estate as a whole).

[5] Before the Committee NH claimed:

a. $6,690.13 in legal fees incurred in seeking advice in respect of this matter;

b. $4,659.54 which was an amount that he forgave NF as he said it was unrecoverable;

c. An adjustment in respect of the date of the valuation of the entitlements to be the date of the distribution rather than the date of the death of the testatrix; and

d. An adjustment representing a refund of the fees deducted from the estate when TW acted inappropriately without reference to NH.

[6] The Committee did not adopt NH's framework when it made its Orders. Rather it recalculated NH's entitlement and reached the conclusion that his proper entitlement was $215,287.05. That amounted to the value of his interest, discounted for the life expectancy of NF, and deducting a portion of the estate's properly payable legal costs. The amount in fact paid was $204,603.35. The Committee therefore considered that NH had been underpaid $10,683.70 and ordered that amount to be paid in compensation.

[7] Thus in respect of the claims of NH the Committee:-

a. Ordered compensation of $4,500.00 in legal fees incurred in seeking advice in respect of this matter;

b. Accepted that NH was entitled to the full value of his interest in the estate but to include the $4,659.00 in the global assessment of value (and did not deal with it separately);

c. Considered that an adjustment in respect of the date of the valuation of the entitlements to be the date of the distribution rather than the date of the death of the testatrix was appropriate;

d. Considered that an adjustment representing a refund of the fees deducted from the estate when TW acted inappropriately without reference to NH was not appropriate.

[8] The Standards Committee made a finding of unsatisfactory conduct on the part of TW when he advanced capital to NF without reference to NH. No review is sought in respect of this finding.

[9] However, TW sought a review only of the Orders made (and in particular the Orders relating to compensation/legal fees).

[10] The main arguments of TW on review were:

a. NH was not compelled to compromise his entitlement and could have pursued his father for the outstanding amount and therefore the sum of $4,659.00 should not be included in any settlement amount.

b. That the proper date of valuation of the interests of the parties was the date of death of the testatrix and not the date of the settlement between NF and NH.

c. That income received by the estate between the date of the death of the testatrix and the date of the settlement between NH and NF was properly payable to NF absolutely and the Committee should not have taken that into account in determining the entitlement of NH.

d. That the Committee wrongly concluded that TW had suggested that compensation of $4,500.00 in respect of legal fees was appropriate when in fact this was an amount suggested as compensation for all matters.

[11] In response to the submissions of TW, NH stated that he decided to settle the issue of his entitlements under the Will with his father (NF) for less than his entitlement under the Will, due to the fact that his father was not in a position to return the balance of the funds and he sought a pragmatic solution to the problem by relinquishing a portion of his entitlement against his father to secure settlement.

[12] He also stated that the date of the distribution is the proper date for valuation, noting that for a significant period of time NF had the benefit (interest free) of the capital of a portion of the estate.

Analysis

[13] The power to make an Order of compensation is found in s 156(d) of the Lawyers and Conveyancers Act 2006. That section provides that the Standards Committee may order compensation where it appears "…that any person has suffered loss by reason of any act or omission of a practitioner".

[14] It appears to be accepted that some loss has been suffered by NH by the conduct of TW. The issue is the exact quantum of that loss. In particular, what loss was caused by TW (i.e. was suffered 'by reason of' an act or omission of TW) and what losses, costs and expenses would have been incurred anyway.

The $4,659.00 shortfall

[15] The suggestion that NH ought not to be compensated for the loss of that part of his interest that he relinquished in order to achieve settlement is not sustainable. The position in which NH found himself (i.e. that his entitlement was at risk due to the advance of the capital to the life interest holder) was due to the conduct of TW. He was entitled to take reasonable steps to mitigate that fact. Directly relevant is that the capital had been advanced on an unsecured loan to NF and that NF was unable to repay it. Although he may have had assets from which payment could be sought, it was open to NH to elect whether to pursue the shortfall from the assets of NF (or presumably from his estate on NF's death when the entitlement crystallised), or to seek to secure as much of his entitlement as immediately possible to recover, and to seek to recover the shortfall from TW as the wrongdoer.

[16] In this regard the Committee was correct to include the amount of compensation for the diminished value of the interest, the $4,659.00 less that NH received.

Date of valuation of interests

[17] The date of the valuation of the interests as between NF and NH is important (or more accurately the age of NF at the time of the valuation of the interests is important). Where the holder of a life interest is aged 71 the interest of the remainderman (in accordance with the table found in schedule 2 of the Estate and Gift Duties Act 1968) is 0.62834 of the whole. If the holder of the life interest is aged 73 the value of the remainder is 0.66040 of the whole. In the present case (assuming the value of the life interest to be $327,685.41) the difference is some $10,505.59.

[18] TW is correct when he states that it is "trite" that the proper date for the valuation of an interest under a will is the date of death. However, the distribution in this case was not in fact a distribution under a will in that sense. Rather it was a settlement of an issue which had arisen due to the wrongful payment of capital to the life interest holder by TW. While the interests valued arose under the Will, the distribution was a settlement of those interests. In such situations the proper date for the valuation of the interests was the date upon which the settlement was reached and the life interest and remainder were converted to respective interests in the capital.

[19] The purpose of valuation of the life interest is to take account of the uncertainty as to the date of death and therefore the date at which the capital will pass to the remainderman. When it was determined some two years after the date of the death of the testatrix that the rights of the parties would be valued and paid there was no possibility that NF would die in the preceding two years. It would therefore be perverse to reduce the amount payable to NH to take that into account.

[20] It is also the case that if the date of valuation was the date of death of the testatrix then the proper time for distribution to NH would have been as soon as possible after death. As NH points out, in fact the benefit of the funds was given to NF for this period and NF did not receive any funds until late in 2010. Had NH received the funds earlier he would have had the benefit of the income for this period (and of any capital appreciation that might have occurred).

[21] The lack of tenability of the position of TW is further demonstrated by considering what would have happened if the $250,000.00 advance had not been discovered for a further ten years and the valuation of the life interest which was being realised was correspondingly significantly higher. It would be contrary to principle to value the interest being capitalised retrospectively in such a case. It is correspondingly contrary to principle to do so in this case.

[22] I conclude that the Standards Committee was correct to value the interests of NF and NH at the time that NF was aged 73.

Appropriation of income between date of death and date of valuation

[23] TW argues that because NF was the life interest holder he was entitled to any income of the estate prior to the date of valuation. This included interest accrued. Because NH was only a remainderman he ought not to be entitled to the benefit of any interest, but only to the value of the capital as at the date of settlement.

[24] From a “Distribution Summary” provided by TW it appears that as at 25 February 2010 the estate had received income of $18,802.25 and held as capital a further $964,253.99 (in which NF had a 1/3 life interest).

[25] NH objects that NF had the benefit of an interest free loan of $250,000.00 and therefore ought to not also be entitled to a third of the interest on the assets of the estate. This may well be correct - as between the various beneficiaries it may be that the interests of NF ought to be reduced to reflect the fact that at that time he appeared to be in control of a large portion of the fund in which he had an interest and may not

be entitled, as against the other beneficiaries, to a 1/3 share of the interest of the remaining assets.

[26] However this does not mean that NH is entitled to the income of the fund between the date of death of the testatrix and the date of the settlement of his entitlement. TW is correct in stating that the income of the estate up to the date of the valuation and settlement of the life interest and remainder as between NH and NF was payable to the estate and did not form part of the remainder to which NH was entitled.

[27] Accordingly I accept that at the time of the valuation of the life interest the value of the life interest was 1/3 of $964,253.99 (namely $321,417.99 and not the $327,685.41 which was used by the Committee as the basis of its calculations). However, I consider that the objection of NH has some merit. In particular, in investing funds in respect of which there is both a life interest and a remainder, the interests of both parties are to be taken into account.

[28] A trustee is obliged to ensure that the capital of an estate is preserved, including protecting it against erosion from inflationary pressures. In the present case TW appears to have assumed the role of trustee by making decisions in respect of the investment of the funds of the estate, including advancing them to NF and holding them on fixed interest bearing deposits. It does not appear that any allowance or provision was made to ensure that the capital of the fund was not diminished in real value due to inflation. In this regard TW, if managing the funds of the estate, was obliged to act fairly as between NF and NH as the life beneficiary and the remainderman respectively (*Nestle v National Westminster Bank plc* [1994] 1 All ER 118 at pp 4-5). Although it is of note that in the present case the funds were held for a relatively short period of time (some two years), there is authority to suggest that trust funds ought not to be held solely in fixed interest bearing investments where there is an obligation to reasonably and fairly protect the interest of a remainderman (*Re Mulligan (Deceased)* [1998] 1 NZLR 481 (HC)).

[29] I consider it appropriate that some allowance be made for this failure. At the relevant time inflation (as measured by the Consumer Price Index in 2010 was between 1.5 and 4 per cent per annum).

[30] If the capital had been preserved by proper investment it might be expected to have increased by at least 2 per cent per annum (or some $6553.37 per annum).

[31] I note that the matter appears to have in fact been outstanding for almost two years (between December 2009 and 20 October 2011) and that the capital had not been preserved from the effects of inflation for that period.

[32] Given the above analysis it is arguable that there should be some upward adjustment of the compensation payable by TW to take account of the fact that in real terms the capital reduced in value over the two years it was under his stewardship. However, this was not a point directly raised by NH who did not seek a review of the decision or any aspect of it and as such I do not think that it is necessary to make that adjustment.

[33] However, in light of this I do not consider that it is appropriate to make any adjustment in the amount of compensation in light of the attribution of the Standards Committee of income to capital in these circumstances.

Legal costs

[34] The Committee considered that some compensation for legal costs incurred by NH was appropriate. However it did not accept that payment of the full amount claimed of $6,690.00 was proper. In ordering compensation of $4,500.00 in respect of legal fees it stated that TW had agreed that this was a reasonable amount to compensate for that. TW states that his suggestion that compensation of $4,500.00 would be reasonable (made in his letter of 19 May 2011) related to all of the matters in dispute and not just to legal costs.

[35] Having read that letter it is fair to say that the Committee's interpretation of it was a reasonable one and cannot be said to be erroneous. The letter has two numbered points and the comment that "payment of $4,500.00 is an appropriate level of compensation" is linked to the discussion of legal costs.

[36] Even if the statement was not a concession intended by TW that $4,500.00 is an appropriate level of compensation for legal costs, it is clearly appropriate that TW bear the reasonable costs of NH which he incurred in pursuing this matter. Similarly it is proper that full costs are not given as compensation because, as the Committee noted, some costs would necessarily have been incurred in arranging for the valuation of and payment out of the remainder.

[37] The proper question is what proportion of the legal costs should be shared between TW and NH. Putting aside the approach of the Committee as to TW's submission, the Order of the Committee that TW bear $4,500.00 of the costs and NH bear the remaining $2,190.00 appears to be a reasonable split in all of the circumstances and could have properly been made quite apart from the argument of TW that the statement in his letter was misinterpreted.

[38] I consider that the compensation Order of $4,500.00 in respect of legal costs is appropriate.

Fees of the Estate

[39] I note that the Committee did not accept that there should be some rebate of fees that were paid from the capital of the estate in respect of TW's costs. It found that TW was entitled to take his costs that were reasonably incurred (and would have been incurred in any event). This appears to have been a reasonable approach of the Committee.

Conclusion

[40] I consider that in all of the circumstances the Orders of the Committee as to penalty are an appropriate assessment of the loss that NH has suffered by reason of the acts or omissions of TW. For that reason the Orders of the Committee should stand.

Costs of review

[41] It is appropriate that an Order of costs be made in respect of the conduct of this review. By s 210(3) of the Lawyers and Conveyancers Act an Order of costs may be made in respect of the costs of this Office whether or not a finding of unsatisfactory conduct has been made where it appears just to do so.

[42] In the present case there has been some minor adjustment to the way in which the compensation amounts are reached. However I have concluded that there should be no adjustment to the amounts payable in compensation by TW.

[43] Accordingly it is appropriate that TW pay some portion of the costs of this review. The Costs Order Guidelines of this Office would suggest that where a review is of medium complexity and is conducted on the papers that an Order of $1,200.00 would be appropriate. In the circumstances I consider that a modest discount from that sum is sensible and that an Order of costs in the sum of $900.00 is appropriate.

Decision

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

Pursuant to s 210(3) of the Lawyers and Conveyancers Act, TW is ordered to pay to the New Zealand Law Society the sum of $900.00 in respect of the conduct of this review, to be paid within 30 days of this decision.

DATED this 21st day of February 2013

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Hanneke Bouchier
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:

TW as the Applicant
NH as the Respondent
MJ as a related person or entity as a requirement under s 213 of the Act
The Otago Standards Committee
The New Zealand Law Society