



Ethics for Trust and Estate Practitioners: Managing Conflicts of Interest

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Agenda

- **Part I:** Conflicts of Interest Between Clients - The Perils of Joint Retainer Agreements
- **Part II:** Managing Conflicts that Arise When A Lawyer Acts in their Capacity as Both Legal Advisor and Executor, Power of Attorney or Trustee
- **Part III:** Managing Conflicts of Interest that Arise When A Lawyer Acts in the Capacity as Both Legal Advisor and Director of a Corporation in Which the Client or Related Party Has an Interest



Part I

Conflicts of Interest Between Clients:

The Perils of Joint Retainer Agreements



Fact Scenario

Mr. and Mrs. Simpson come in to see you. They have been married for approximately 15 years. It is a second marriage for both, and each has one adult child from a prior relationship. They do not have children together.

They tell you that they want mirror wills, with the estate of the first to die payable to the surviving spouse. When you meet them together, they tell you that on the last to die, they want their estates split in two equal shares to their respective children. You draw wills for them containing these provisions and the wills are executed.



Joint Retainers: Starting off on the Right Foot

- Embedded in the duty of loyalty, the duty of commitment to a client's cause, and the duty of candour is the duty to give all relevant information to your client in respect of a retainer. In other words, you have a duty to tell them everything. The minute you get information from one client that is pertinent to the other, on a joint retainer, you must disclose.
- The only way you can ever act for a husband and wife who are potentially adverse in interest is to secure informed consent.



How to deal with ethical issues arising on joint retainers

- To avoid conflicts completely, avoid acting for two spouses in a blended family scenario. Act for one spouse and refer other spouse out for separate representation.
- If you must act, you must explain potential for conflict in person, and follow up in writing. Retainer letters for joint retainers should always contain an explanation of the nature of the joint retainer and the duty of loyalty to both clients.
- Duties arise as soon as you speak on the phone with someone.



How to deal with ethical issues arising on joint retainers cont'd

- Find out all of the facts on the phone before setting up a meeting with someone.
- Sometimes it is a good idea to suggest meeting alone with the client who calls you and then decide whether it can be a joint retainer. This avoids being in a position where you discover a conflict only once you are in a position where you have met with both and can act for neither.



Joint Retainers: The Ethical Framework: BC Code of Professional Conduct

3.4-5 Before a lawyer is retained by more than one client in a matter or transaction, the lawyer must advise each of the clients that:

- (a) the lawyer has been asked to act for both or all of them;
- (b) no information received in connection with the matter from one client can be treated as confidential so far as any of the others are concerned; and
- (c) if a conflict develops that cannot be resolved, the lawyer cannot continue to act for both or all of them and may have to withdraw completely.



Joint Retainers

LSUC Rules of Professional Conduct

Rule 2 – Relationship to Clients

2.04 Avoidance of Conflicts of Interest

- (6) Except as provided in subrule (8.2), where a lawyer accepts employment from more than one client in a matter or transaction, the lawyer shall advise the clients that
- a) the lawyer has been asked to act for both or all of them,
 - b) no information received in connection with the matter from one can be treated as confidential so far as any of the others are concerned, and
 - c) if a conflict develops that cannot be resolved, the lawyer cannot continue to act for both or all of them and may have to withdraw completely.



Commentary

Although this sub-rule does not require that, before accepting a joint retainer, a lawyer advise the client to obtain independent legal advice about the joint retainer, in some cases, especially those in which one of the clients is less sophisticated or more vulnerable than the other, the lawyer should recommend such advice to ensure that the client's consent to the joint retainer is informed, genuine, and uncoerced.

A lawyer who receives instructions from spouses or partners as defined in the *Substitute Decisions Act, 1992 S.O. 1992 c. 30* to prepare one or more wills for them based on their shared understanding of what is to be in each will should treat the matter as a joint retainer and comply with subrule (6).



Commentary (Cont'd)

Further, at the outset of this joint retainer, the lawyer should advise the spouses or partners that if subsequently only one of them were to communicate new instructions, for example, instructions to change or revoke a will:

- a) the subsequent communication would be treated as a request for a new retainer and not as part of the joint retainer;
- b) in accordance with rule 2.03, the lawyer would be obliged to hold the subsequent communication in strict confidence and not disclose it to the other spouse or partner; but



Commentary

c) the lawyer would have a duty to decline the new retainer, unless;

- i. the spouses or partners had annulled their marriage, divorced, permanently ended their conjugal relationship, or permanently ended their close personal relationship, as the case may be;
- ii. the other spouse or partner had died; or
- iii. the other spouse or partner was informed of the subsequent communication and agreed to the lawyer acting on the new instructions.

After advising the spouses or partners in the manner described above, the lawyer should obtain their consent to act in accordance with subrule (8).



Joint Retainers (Cont'd)

- (9) Save as provided by subrule (10), where clients have consented to a joint retainer and an issue contentious between them or some of them arises, the lawyer shall
- a) not advise them on the contentious issue, and
 - b) Refer the clients to other lawyers, unless
 - i. no legal advice is required, and
 - ii. the clients are sophisticated, in which case, the clients may settle the contentious issue by direct negotiation in which the lawyer does not participate.
- (10) Where clients consent to a joint retainer and also agree that if a contentious issue arises the lawyer may continue to advise one of them and a contentious issues does arise, the lawyer may advise the one client about the contentious matter and shall refer the other or others to another lawyer.



Joint Retainers: Provisions in the NS *Code of Professional Conduct*

Rule 3.4 Duty to Avoid Conflicts of Interest

3.4-5 Before a lawyer acts in a matter or transaction for more than one client, the lawyer must advise each of the clients that:

- (a) the lawyer has been asked to act for both or all of them;
- (b) no information received in connection with the matter from one client can be treated as confidential so far as any of the others are concerned; and
- (c) if a conflict develops that cannot be resolved, the lawyer cannot continue to act for both or all of them and may have to withdraw completely.



Commentary

- [1] Although this rule does not require that a lawyer advise clients to obtain independent legal advice before the lawyer may accept a joint retainer, in some cases, the lawyer should recommend such advice to ensure that the clients' consent to the joint retainer is informed, genuine and uncoerced. This is especially so when one of the clients is less sophisticated or more vulnerable than the other.
- [2] A lawyer who receives instructions from spouses or partners to prepare one or more wills for them based on their shared understanding of what is to be in each will should treat the matter as a joint retainer and comply with rule 3.4-5. Further, at the outset of this joint retainer, the lawyer should advise the spouses or partners that, if subsequently only one of them were to communicate new instructions, such as instructions to change or revoke a will:



Commentary (Cont'd)

- (a) the subsequent communication would be treated as a request for a new retainer and not as part of the joint retainer;
- (b) in accordance with section 3.3, the lawyer would be obliged to hold the subsequent communication in strict confidence and not disclose it to the other spouse or partner; and
- (c) the lawyer would have a duty to decline the new retainer, unless:
 - (i) the spouses or partners had annulled their marriage, divorced, permanently ended their conjugal relationship or permanently ended their close personal relationship, as the case may be;
 - (ii) the other spouse or partner had died; or
 - (iii) the other spouse or partner was informed of the subsequent communication and agreed to the lawyer acting on the new instructions.



Commentary (Cont'd)

[3] After advising the spouses or partners in the manner described above, the lawyer should obtain their consent to act in accordance with rule 3.4-9.

- 3.4-8** Except as provided by rule 3.4-9, if a contentious issue arises between clients who have consented to a joint retainer, the lawyer must not advise them on the contentious issue and must:
- (a) refer the clients to other lawyers; or
 - (b) advise the clients of their option to settle the contentious issue by direct negotiation in which the lawyer does not participate provided:
 - (i) no legal advice is required; and
 - (ii) the clients are sophisticated



Joint Retainers (Cont'd)

- **3.4-8A** If the contentious issues referred to in rule 3.4-10 are not resolved, the lawyer must withdraw from the joint representation.



Commentary

- [1] This rule does not prevent a lawyer from arbitrating or settling, or attempting to arbitrate or settle, a dispute between two or more clients or former clients who are not under any legal disability and who wish to submit the dispute to the lawyer.
- [2] If, after the clients have consented to a joint retainer, an issue contentious between them or some of them arises, the lawyer is not necessarily precluded from advising them on non- contentious matters.



Joint Retainers (Cont'd)

3.4-9 Subject to this rule, if clients consent to a joint retainer and also agree that, if a contentious issue arises, the lawyer may continue to advise one of them, the lawyer may advise that client about the contentious matter and must refer the other or others to another lawyer.



Commentary

- [1] This rule does not relieve the lawyer of the obligation, when the contentious issue arises, to obtain the consent of the clients when there is or is likely to be a conflict of interest, or if the representation on the contentious issue requires the lawyer to act against one of the clients.
- [2] When entering into a joint retainer, the lawyer should stipulate that, if a contentious issue develops, the lawyer will be compelled to cease acting altogether unless, at the time the contentious issue develops, all parties consent to the lawyer's continuing to represent one of them. Consent given before the fact may be ineffective since the party granting the consent will not at that time be in possession of all relevant information.



FACT SCENARIO (cont.)

Three years after the wills are executed, Mrs. Simpson contacts you. She has had a falling out with Mr. Simpson's son, Jake. Mr. Simpson has developed advanced dementia and has moved into an assisted living facility. Jake feels that Mrs. Simpson should sell the family home (owned in joint tenancy by Mr. and Mrs. Simpson) and move into an apartment. He has told her it is wasteful for Mrs. Simpson to be spending "his inheritance" on the upkeep of such a large home. Mrs. Simpson suspects that Jake is abusing illegal drugs and she is both hurt and offended by what she perceives as his aggressive behaviour to her. She wants you to draft a new will for her that will leave nothing to Jake and will provide that in the event Mr. Simpson predeceases Mrs. Simpson, Mrs. Simpson's estate will pass in its entirety to her daughter.

Can you prepare the will for her?



Commentary to Section 3.4-5 of the B.C. Code

A lawyer who receives instructions from spouses or partners to prepare one or more wills for them based on their shared understanding of what is to be in each will should advise the spouses or partners that, if subsequently only one of them were to communicate new instructions, such as instructions to change or revoke a will:

- (a) the subsequent communication would be treated as a request for a new retainer and not as part of the joint retainer;
- (b) in accordance with rule 3.3-1, the lawyer would be obliged to hold the subsequent communication in strict confidence and not disclose it to the other spouse or partner; and



Commentary to Section 3.4-5 of the B.C. Code (Cont'd)

(c) the lawyer would have a duty to decline the new retainer, unless: (i) the spouses or partners had annulled their marriage, divorced, permanently ended their conjugal relationship or permanently ended their close personal relationship, as the case may be; (ii) the other spouse or partner had died; or (iii) the other spouse or partner was informed of the subsequent communication and agreed to the lawyer acting on the new instructions.



Application of B.C. Code to Facts

- Must decline retainer and keep communication confidential from Mr. Simpson unless (1) instructed to disclose and (2) able to obtain Mr. Simpson's informed consent.
- Given Mr. Simpson's diminished capacity, informed consent unlikely on these facts.
- How does analysis change if Mr. Simpson and Mrs. Simpson have divorced? Any barriers to acting for Mrs. Simpson?
- Under BC Code, probably ok, so long as it is treated like a new retainer.



Joint Retainers: Is there such a thing as the “Family’s Lawyer”

- Short answer: no. Pretty much impossible to act for more than one generation and not be in a conflict of interest.
- If acting for matriarch/patriarch, you are not acting for the children.
- This doesn’t mean no family meetings, but must be made clear to kids that you are not their lawyer.



PART II

Managing Conflicts that Arise When A Lawyer Acts in their Capacity as Both Legal Advisor and Executor, Power of Attorney or Trustee



Overview

- Situations where lawyers find themselves in conflicts of interest with their clients
- Provisions from the Nova Scotia *Code of Professional Conduct* (the “Code”)
- Obligations of a drafting lawyer when:
 - Drafting wills for a client and acting as executor
 - Drafting powers of attorney for a client and being appointed as attorney
 - Drafting a trust for a client and acting as either settlor or as trustee of the trust
- Lawyer as witness to the instrument and later in court



Conflicts of Interest Situations

- Lawyers may find themselves in conflicts of interest with their clients in any of the following situations:
 - Drafting wills for a client and acting as executor
 - Drafting powers of attorney for a client and being appointed as attorney
 - Drafting a trust for a client and acting as either settlor or trustee
- While this is not strictly prohibited under the NS Code, lawyers must be careful when wearing multiple hats



NS Code of Professional Conduct Provisions

- The “new” conflict of interest provisions were adopted under the *NS Code* in July 2012.
- **Duty to Avoid Conflicts of Interest**

3.4-1 A lawyer must not act or continue to act for a client where there is a conflict of interest, except as permitted under this Code.

Commentary: A conflict of interest exists when there is a **substantial risk** that a lawyer’s loyalty to or representation of a client would be materially and adversely affected by the lawyer’s own interest or the lawyer’s duties to another client, a former client, or a third person...



NS Code of Professional Conduct Provisions

- Rule 3.4-2 provides an exception permitting a lawyer to act where there is express or implied consent from clients and the lawyer reasonably believes that he or she is able to represent each client without there being any material adverse effect upon either the representation of or the loyalty to the clients.



LSUC – Rules of Professional Conduct

Rule 2: Relationship to Clients

2.04 Avoidance of Conflicts of Interest

2.04 (1) In this rule

A “conflict of interest” or a “conflicting interest” means an interest

(a) that would be likely to affect adversely a lawyer’s judgment on behalf of, or loyalty to, a client or prospective client, or

(b) that a lawyer might be prompted to prefer to the interests of a client or prospective client.

(2) A lawyer shall not advise or represent more than one side of a dispute.

(3) A lawyer **shall not act or continue to act in a matter when there is or is likely to be a conflicting interest** unless, after disclosure adequate to make an informed decision, the client or prospective client consents.



NS Code of Professional Conduct Provisions

- **Retainers as Solicitor for the Estate**

3.4-37 A lawyer must not include in a client's will a clause directing the executor to retain the lawyer's services in the administration of the client's estate.

- While solicitors often expect to be retained by the executors to act on their behalf in administering the estate, including such a directive clause in the will is improper
- It may also cause future conflicts of interest: for example between duties to the executor and the beneficiaries. These conflicts could be compounded if the executor is also a beneficiary.



NS Code of Professional Conduct Provisions

- Testamentary Instruments and Gifts

3.4-28 Subject to this rule, a lawyer must not enter into a transaction with a client unless the transaction is fair and reasonable to the client, the client consents to the transaction and the client has independent legal representation with respect to the transaction.

- **Commentary: [1]** This provision applies to any transaction with a client, including: ... (c) **accepting a gift, including a testamentary gift;**
- **[2]** ...The remuneration paid to a lawyer by a client for the legal work undertaken by the lawyer for the client does not give rise to a conflicting interest. **Note – does not expressly exclude executor compensation in the Commentary.**



NS Code of Professional Conduct Provisions

3.4-38 Unless the client is a family member of the lawyer or the lawyer's partner or associate, a lawyer must not prepare or cause to be prepared an instrument giving the lawyer or an associate a **gift or benefit** from the client, **including a testamentary gift**.

3.4-39 A lawyer must not accept a gift that is more than nominal from a client unless the client has received independent legal advice ("ILA") (definition of ILA, **3.4-27**)



LSUC Rules of Professional Conduct

(Note: the following provisions are from the proposed amended rules implementing the Federation of Law Societies of Canada's Model Code of Professional Conduct, which will become effective on October 1, 2014.)

- 3.4-28 Subject to this rule, a lawyer must not enter into a transaction with a client unless the transaction is fair and reasonable to the client, the client consents to the transaction and the client has independent legal representation with respect to the transaction...
(c) accepting a gift, including a testamentary gift;



LSUC Rules of Professional Conduct (Cont'd)

Testamentary Instruments and Gifts

- 3.4-37 If a will contains a clause directing that the lawyer who drafted the will be retained to provide services in the administration of the client's estate, the lawyer should, before accepting that retainer, provide the trustees with advice, in writing, that the clause is a non-binding direction and the trustees can decide to retain other counsel.
- 3.4-38 Unless the client is a family member of the lawyer or the lawyer's partner or associate, a lawyer must not prepare or cause to be prepared an instrument giving the lawyer or an associate a gift or benefit from the client, including a testamentary gift.
- 3.4-39 [FLSC - not in use] → no equivalent provision in the Ontario Code to 3.4-39 in NS/BC Codes.



Code of Professional Conduct for British Columbia

Note: The provisions are analogous to the Nova Scotia Code.

- 3.4-28 Subject to this rule, a lawyer must not enter into a transaction with a client unless the transaction is fair and reasonable to the client, the client consents to the transaction and the client has independent legal representation with respect to the transaction ...
(c) accepting a gift, including a testamentary gift;



Code of Professional Conduct for BC (Cont'd)

Testamentary Instruments and Gifts

- 3.4-37 A lawyer must not include in a client's will a clause directing the executor to retain the lawyer's services in the administration of the client's estate.
- 3.4-38 Unless the client is a family member of the lawyer or the lawyer's partner or associate, a lawyer must not prepare or cause to be prepared an instrument giving the lawyer or an associate a gift or benefit from the client, including a testamentary gift.
- 3.4-39 A lawyer must not accept a gift that is more than nominal from a client unless the client has received independent legal advice.



Drafting Wills and Acting as Executor

- “Benefit” is not defined within the Code and, depending on its interpretation, Rule 3.4-38 could preclude a lawyer from drafting a will in which he or she is appointed as executor.
- The Regulation Committee of the Law Society of Upper Canada stated that Rule 3.4-38 (identical to the NS rule) would not preclude the appointment of drafting lawyers as executors.





Drafting Wills and Acting as Executor

A portion of the meeting transcript reads:

“With respect to 3.4-38, the lawyer can’t draft or cause to be drafted an instrument giving the lawyer or their associate a gift or benefit, including a testamentary gift. It’s important that we not be doing the lawyering and be the beneficiaries of the gifts and benefits when we’re doing the lawyering. That’s contrary to the conflicts rule...

...[a]n executorship is not a gift or a benefit.”



Drafting Wills and Acting as Executor

- A disproportionate number of cases in which lawyers are disciplined for breaching the duty to serve clients conscientiously arise out of retainers to administer estates, particularly in cases where the lawyer serves also as executor of the estate, and the beneficiaries live far away or do not know that they have been left any interest in the testator's estate.¹

¹ G MacKenzie, *Lawyers and Ethics: Professional Responsibility and Discipline*, 4th ed (Toronto: Thomson Carswell, 2006) at 18-9.



Exoneration clauses

- Similar concerns arise in respect of an exoneration clause added to a will which the lawyer drafts when the executor/trustee named in the will who could be exonerated is the drafting lawyer!
- Is this only an issue if the clause purports to exonerate everything but fraud and gross negligence?
- Does this clause present an ethical issue?

My trustees will not be responsible for any error in judgment or for any act of omission or commission not amounting to wilful default or actual fraud in the management and administration of my estate or any trust established in this will. My trustees will be entitled to be indemnified by my estate or any trust established in this will for all expenses and liabilities howsoever arising out of the performance in good faith of their duties as trustees.



Hypothetical

- A long-time client and friend with substantial wealth and little close family comes to you requesting that you draw up their Will.
- Upon discussing executor's fees and suggesting a trust company, your client insists that she wants you to oversee and attend to her affairs after death, and that she wants to pay you more than 5% commission.
- She insists on this, and also insists that you leave a \$10,000 gift to yourself in the will.
- Despite advising your client that you cannot accept the gift in your role as solicitor unless she obtains ILA, your client refuses.
- You agree to include the gift in the will, believing that it would not be paid (under provisions in the *Probate Act* preventing you from receiving more than the 5% fixed commission).
- You prepare the will accordingly, and it is properly executed.



Hypothetical cont'd

- A few years later following the death of your client's primary beneficiaries under the will, she asks you to prepare a new will.
- She wants to increase the gift to you.
- You suggest that the will be changed from 5% commission to a 5% "bequest in lieu of commission," as permitted under the *Probate Act*.
- The \$10,000 bequest is removed.
- Your client is pleased.
- At this point you do not consider suggesting ILA, thinking this is permitted at law.
- The will is properly executed and witnessed.
- Upon death of your client the will is probated and distributions made, including the "bequest in lieu of commission" to you.
- What happens next?



The Importance of Independent Legal Advice

Many examples of disciplinary proceedings arising out of a lawyer receiving testamentary gifts

- This fact pattern comprised *Nova Scotia Barristers' Society v. Muttart*, 2009 NSBS 4, where Muttart, the drafting lawyer, was found guilty of professional misconduct for preparing a will in which he received the substantial testamentary gift in lieu of commission and the client did not have independent legal advice regarding the disposition.
- Received a reprimand and had to pay costs



The Importance of Independent Legal Advice

- In *Nova Scotia Barristers' Society v. Romney*, 2004 NSBS 7, the Hearing panel found that in accepting “gifts” from elderly clients of cash, property and other assets, including joint ownership of an investment account, without independent legal advice, Romney was in a conflict of interest, even in the face of evidence that the cash and assets were given to Romney from the clients voluntarily.
- The Panel also noted that the then rules required that independent legal advice be obtained, even if the clients expressed no interest in doing so.



The Importance of Independent Legal Advice

- Ethics committees have stressed on many occasions that the interests of, and loyalty to, the client must be **paramount**.
- If it is believed a lawyer's actions are being driven by personal interests, and not the client's, the lawyer should withdraw
 - (NS Legal Ethics Committee Minutes (13 November 1997)).
- If the client is advised to obtain ILA and waives it, that should be documented.



Acting as Trustee or Attorney

- Lawyer-client conflicts arise when a lawyer takes possession of client assets when acting as trustee or attorney.
- When lawyers maintain client trust accounts or property, they are placed under significant fiduciary obligations to take special care of their client's money and property and to account for it appropriately – the law societies have reporting and audit powers to ensure compliance.
- It is important that clients can place a high degree of confidence in their lawyers.
- It is therefore not surprising that lawyers who abuse their client's trust by misappropriating trust monies for their personal use are dealt with harshly by law societies and the courts!



NS Trust Account Regulations When Acting in a Representative Capacity

- 10.1.2 A lawyer is acting in a representative capacity if the lawyer is
- (a) the personal representative, executor or administrator, or one of the personal representatives, executors or administrators, of the estate of a deceased person;
 - (b) a trustee, or one of the trustees, of a trust under an appointment made pursuant to a trust instrument creating the trust;
 - (c) a trustee, or one of the trustees, of the property of another person under an appointment by a court;
 - (d) a de facto trustee; or
 - (e) an attorney, or one of the attorneys, of a person under a power of attorney, whether general or special, enduring or otherwise.



NS Trust Account Regulations When Acting in a Representative Capacity

10.1.3 A lawyer is not required to deposit trust money or trust property received by a lawyer acting in a representative capacity into the lawyer's or law firm's trust account or record the trust money or trust property in the prescribed financial records of the lawyer's law firm if

(a) the lawyer maintains a record of all appointments or assumptions of a representative capacity and a list of the beneficiaries of the estate or trust together with their last known address;

(b) the books, records, accounts and documentation of the estate or trust are in a form sufficient to accommodate an examination, review, audit or investigation ordered by the Executive Director or Complaints Investigation Committee; and

(c) the lawyer or law firm cooperates with the Society's auditor or investigator in the conduct of any examination, review, audit or investigation so ordered.



Compensation Issues when a Solicitor is Named Executor or Trustee:

- A lawyer–trustee/executor who seeks both professional fees and trustee’s compensation has an obligation to satisfy the beneficiaries and the Court that the full consequences of the arrangement were explained to the testator/settlor.
 - See *Estate of Roman Krentz*, 2011 ONSC 1653
- Lawyers should fully explain to clients the manner in which trustees may claim compensation, and the potential for “double dipping” if the client names a lawyer as trustee.
- ILA is no longer expressly required but should be suggested regardless of manner of compensation (hourly rate, compensation agreement, fixed percentage etc.)
- A conflict letter outlining the manner of compensation should be sent to the client with the draft documents.



Re Rustig Estate, 2002 NSSC 210

- **Para 23:** The Saskatchewan Court of Appeal confirmed the proposition that a solicitor acting as an executor cannot charge full professional fees for non-professional executor's duties. In *Re McIntosh* (1964), 46 D.L.R. (2d) 416, Maguire, J. wrote at p. 418:

"It has long been established that a professional man, be he solicitor, accountant or otherwise, will not be granted compensation on the basis of professional charges for services rendered in respect of those services not actually professional in nature, which an executor not being a solicitor, could perform without legal advice."

- **Para 24:** Where an executor also acts as proctor under the authority of the will or with the full consent of co-executors, separate recording of the duties exercised and preferably in separate and distinct logs, one covering the time and services as executor and the other, the normal docket recording professional legal services.
- **Para 34** ...the court in determining entitlement and the quantum of the commission should examine the extent to which the executor has, under the authority of the will, sought payment for services that were not necessarily legal but administrative on a professional legal fee basis.



Drafting a Trust and acting as Settlor

- Different issues arise when a drafting lawyer is named as settlor, as this requires them to transfer legal ownership of assets to the trustees.
- A relevant Code provision is :
 - **3.4-28** A lawyer must not enter into a transaction with a client unless the transaction is fair and reasonable to the client, the client consents to the transaction and the client has independent legal representation with respect to the transaction.
- Is settling a trust a “transaction”?
- Is the settlement amount (whether nominal or more significant) really part of the fee for the work to draft the trust?
- If a legal fee for acting as settlor is charged but is nominal, then is there still an ethical issue grounded in the Code, and does that make the settlement voluntary?



The Lawyer as Witness

- Having a lawyer act as witness to a will or trust may not be best practice when that lawyer is also appointed under the document, as it can give rise to conflicts of interest in the future if there are issues arising later pertaining to the document.
- If the lawyer has taken on a role such as executor or trustee, they will also be a party to the proceeding if the document is challenged, resulting in further potential conflicts of interest should the lawyer's firm be acting as lawyers for the estate – see 5.2 of the Code re lawyer as witness in court.



The Lawyer as Witness (Cont'd)

- A lawyer must always be aware of the ethical responsibilities to clients, such as maintaining impartiality, and it can appear that a lawyer was not impartial in a case where a lawyer is appointed as executor, settlor or trustee in a document they themselves drafted and/or witnessed.



PART III

Managing Conflicts of Interest that Arise When A Lawyer Acts in the Capacity as Both Legal Advisor and Director of a Corporation in Which the Client or Related Party Has an Interest



- Lawyers are frequently asked to serve as solicitors for related entities.
- In some instances, lawyers serve not only as legal advisors, but as trustees of family trusts and directors of family businesses.
- The role of solicitor for related entities is sufficiently difficult to reconcile in view of the Law Society of Upper Canada's Rules regarding conflict of interest.
- The conflicts become even more serious where the solicitor serves in other fiduciary capacities.



LSUC – Rules of Professional Conduct

Rule 2: Relationship to Clients

2.04 Avoidance of Conflicts of Interest

2.04 (1) In this rule

A “conflict of interest” or a “conflicting interest” means an interest

(a) that would be likely to affect adversely a lawyer’s judgment on behalf of, or loyalty to, a client or prospective client, or

(b) that a lawyer might be prompted to prefer to the interests of a client or prospective client.

(2) A lawyer shall not advise or represent more than one side of a dispute.

(3) A lawyer **shall not act or continue to act in a matter when there is or is likely to be a conflicting interest** unless, after disclosure adequate to make an informed decision, the client or prospective client consents.



Commentary on Rule 2.04 (3)

- A conflict of interest may arise when a lawyer acts not only as a legal advisor but in another role for the client. For example, there is a dual role when a lawyer or his or her law firm **acts for a public or private corporation** and the **lawyer serves as a director** of the corporation. Lawyers may also serve these dual roles for partnerships, trusts, and other organizations. A dual role may raise a conflict of interest because it may **affect the lawyer's independent judgment and fiduciary obligations** in either or both roles, it may obscure legal advice from business and practical advice, it may **invalidate the protection of lawyer and client privilege**, and it has the potential of disqualifying the lawyer or the law firm from acting for the organization. Before accepting a dual role, a lawyer should consider these factors and discuss them with the client. The lawyer should also consider rule 6.04 (Outside Interests and Practice of Law).



Supreme Court of Canada Views on Conflicts of Interest

- Types of Prejudice Addressed by Conflict of Interest Rules

“The law of conflicts is mainly concerned with two types of prejudice: prejudice as a result of the lawyer's misuse of confidential information obtained from a client; and prejudice arising where the lawyer **"soft peddles" his representation of a client in order to serve his own interests, those of another client, or those of a third person.** As regards these concerns, the law distinguishes between former clients and current clients. The lawyer's main duty to a former client is to refrain from misusing confidential information. With respect to a current client, for whom representation is ongoing, the lawyer must neither misuse confidential information, nor place himself in a situation that jeopardizes effective representation.”¹

¹ *Canadian National Railway Company v. McKercher LLP* 2013 SCC 39 at para. 23



- The second main concern, which arises with respect to current clients, is that the lawyer be an effective representative — that he serve as a zealous advocate for the interests of his client. The lawyer must refrain “from being in a position where it will be systematically unclear whether he performed his fiduciary duty to act in what he perceived to be the best interests” of his client.²
- Effective representation may be threatened in situations where the lawyer is tempted to prefer other interests over those of his client: the lawyer's own interests, those of a current client, of a former client, or of a third person.³

²Citing D. W. M. Waters, M. R. Gillen and L. D. Smith, eds., *Waters' Law of Trusts in Canada* (4th ed. 2012), at p. 968. As the oft-cited Lord Brougham said, "an advocate, in the discharge of his duty, knows but one person in all the world, and that person is his client": *Trial of Queen Caroline* (1821), by J. Nightingale, vol. II, *The Defence*, Part I, at p. 8

³Citing *R. v. Neil*, 2002 SCC 70 at para. 31



Illustration

- You are the trustee of the family trust which owns all the common shares of an Opco which your law firm also represents.
- Your partner informs you that in order to discharge your oversight duties as a trustee, you ought to serve as a director of Opco and cites *Bartlett v. Barclays Bank*.⁴
- You and your firm therefore hold the following positions:
 - a) Solicitor for entrepreneur;
 - b) Trustee of family trust established for family of entrepreneur;
 - c) Solicitor for trustees of family trust;
 - d) Director of Opco; and
 - e) Solicitor for Opco.

⁴ *Bartlett v. Barclays Bank Trust Co. Ltd.* 1977 1 Ch. 515



- In this particular example, the existence of these multiple roles is examined from a number of perspectives:
 1. The lawyer has competing fiduciary obligations;
 2. it obscures issues of solicitor and client privilege, particularly when one of the clients served by the solicitor (the trust and its beneficiaries) may be adverse in interest to the other client as a consequence of actions by the first client (the entrepreneur); and
 3. the lawyer may or may not be insured depending on the role in which the solicitor is serving or the actions taken by the solicitor in a fiduciary capacity.



Is the Lawyer Insured?

Law Pro Insurance Policy No. 2014-001

Professional Liability Insurance for Lawyers

Part III - Exclusions

This POLICY does not apply:

- a) to any CLAIM in any way relating to or arising out of any DISHONEST⁵, fraudulent, criminal or malicious act or omission of an INSURED;
- d) to any CLAIM in any way relating to or arising out of an INSURED providing investment advice and/or services, including without limitation, investment advice and/or services relating to or arising out of a business, commercial, or real property investment, unless as a direct consequence of the performance of PROFESSIONAL SERVICES;
- h) to any CLAIM in any way relating to or arising out of legal fees, accounts or any fee arrangement involving the INSURED, or any CLAIM in any way relating to or arising out of any business venture(s) and/or any investment(s) which does not directly relate to the INSURED's practice of law;

⁵Many of the recent English cases address a DISHONEST breach of trust as lawyers are drafting exculpatory clauses to limit liability to dishonesty and fraud.



LawPro Insurance Policy No. 2014-001

Covered Services

Definitions

dd) PROFESSIONAL SERVICES means the practice of the Law of Canada, its provinces and territories, and specifically, those services performed, or which ought to have been performed, by or on behalf of an INSURED in such INSURED'S capacity as a LAWYER or member of the law society of a RECIPROCATING JURISDICTION (not as a member of the Barreau du Québec), subject to Part II Special Provision A; and shall include, without restricting the generality of the foregoing, those services for which the INSURED is responsible as a LAWYER arising out of such INSURED'S activity as a **trustee, administrator, executor, arbitrator, mediator, patent or trademark agent.**



The Duty of Oversight

- While there is no Canadian jurisprudence offering clarity on the duties of the executors or trustees who act as directors of a corporation controlled by the estate, it is clear that trustees of an estate or trust which control a private Corporation have a duty of oversight.⁶
- Practitioners disagree on whether or not that duty of oversight requires that the trustees elect one or more of them to the board of the controlled corporation. However, should they choose not to serve on the board, the trustees are required to ensure that they receive sufficient information to monitor the affairs of the Board of Directors to protect both the trust property and the beneficiaries.

⁶See *Bartlett v. Barclays Bank Trust Co. Ltd.* 1977 1 Ch. 515



How Does a Trustee Oversee the Affairs of a Private Corporation

- The principle of active oversight was articulated in *Bartlett v. Barclays Bank*:

What the prudent man of business will not do is to content himself with the receipt of such information on the affairs of the company as a shareholder ordinarily receives at annual general meetings. Since he has the power to do so, he will go further and see that he has sufficient information to enable him to make a responsible decision from time to time either to let matters proceed as they are proceeding, or to intervene if he is dissatisfied.⁷

⁷ *Bartlett et al. v. Barclays Bank Trust Co. Ltd.* (Nos. 1 and 2) 1977 1 Ch. 515 at p. 532



Improper Supervision

- In *Re Lucking's Will Trusts*⁸ the defendants were trustees of a will. The trust holdings included a majority holding in a private company. Having acquired knowledge that the managing director was withdrawing substantial sums from the company, the director failed to supervise the managing director's drawings. In an action brought against the trustees by the niece, Justice Cross held that the loss with which he was concerned was the decrease in value of the trust shares in consequence of the over-drawings and that the plaintiff was entitled to recover a proportionate part of this decrease in value. It seems clear that the company itself would have a cause of action against the first defendant in his capacity as director. Nevertheless Cross J. did not think that this precluded an action by the beneficiary in his capacity as a trustee:

⁸[1968] 1 WLR 866



Improper Supervision

“He cannot say that what he knew or ought to have known about the company’s affairs he knew, or ought to have known, simply as a director with a duty to the company and no one else. He was in the position he was partly as a representative of the trust and if insofar as he failed in his duty to the company he also failed in his duty to the trust.”⁹

⁹at p. 875



Matters in Control of the Directors Which May Pose a Conflict When the Solicitor is a Director of a Corporation in which an Estate or Trust is a Shareholder

- The following section details items over which the directors have control, all of which are of critical concern to the Trustees of the trust or estate and some of which could give rise to a cause of action on the part of the Trustees on behalf of the beneficiaries.



Dividends

Control of Income to the Trust or Estate

- The directors declare dividends from the corporation. If an estate is dependent upon an income stream from the corporation, the directors must make the appropriate business decisions on timing and distribution of profits of the business.
- Frequent disputes arise when directors fail to declare dividends in favour of shareholders who have a “legitimate shareholder expectation” of a stream of income.
- These decisions are typically examined in shareholder oppression litigation.

Sutherland v. Birks [2001] O.J. No. 0540, [2003] O.J. No. 2885

Cohen v. Jonco Holdings Ltd. (2005) M.B.C.A. 48, [2005 M.J. No. 126, 2007 MBQB 181, [2007] M.J. No. 263

Clarke et al v. Rossbarger et al (2001) 293 A.R. 223



Bonuses, Management Fees, Directors Fees

- The extraction of large bonuses and management fees has a negative impact on the value of the shares owned by the estate or trust.
- Frequently, the freezor continues to draw down large bonuses or management fees without regard to the value of the services rendered.
- This is one of the most frequent “conflicts” between two clients, namely the freezor and the family trust.

Taylor v. West Midland Bank



Bonuses, Management Fees, Directors Fees

- These issues were addressed in *Taylor v West Midland Bank Trust Co Ltd (No 2)*¹⁰
 - In this instance, parents settled the trust for the benefit of their issue. The trust owned all of the shares of a corporation. Excessive management fees were paid to the parents who were also settlors under the trust. The trust company, which did not have a nominee serving as a director, did nothing and permitted the excessive remuneration.

¹⁰ 1999 WL 33210352 p. 1



Bonuses, Management Fees, Directors Fees

“Stripped to its essentials the allegations come to this: for some thirty years between 1964 and 1994 sums had been paid to the settlers by way of directors' remuneration which were excessive and unreasonable and out of all proportion to the value of the work done by them as directors. This was known to the trustees and was part of a deliberate policy instigated by the settlers and agreed to by the trustees. As a result the assets of the company had been seriously depleted and the value of the shares reduced.”



Bonuses, Management Fees, Directors Fees

- Consider this circumstance if a solicitor had been a trustee of the family trust rather than a financial institution.
- Does the lawyer, as solicitor, for either the settlors or the family trust have any obligations?
- Frequently, solicitors are faced with issues involving compensation paid to the freezer who was initially the person who set in motion the gift or benefits to the beneficiaries of the trust. Nevertheless, it is clear that when a gift has been given, no matter how ungrateful the beneficiaries appear, they clearly have rights, as articulated in *Taylor v West Midland Bank*.



Bonuses, Management Fees, Directors Fees

“Firstly, if the trustees have deliberately pursued a policy of favouring the settlor at the expense of the beneficiary, that at least arguably is dishonest under the *Armitage v. Nurse* approach as I understand it. It is no answer that they are not in any way benefiting themselves, nor that many people might find it difficult to attach any moral opprobrium to a policy of favouring the person whose money it was in the first place. The resonances of King Lear do not change the fact that in law, following the settlement, the parents had no right to anything from the company other than proper remuneration.”

- This raises issues requiring the calculation of “proper remuneration”.



Illustration

Bonuses, Management Fees and Salary

- Commercial real estate valued at \$20M is owned by Holdco, which was frozen some time ago. Father has preference shares valued at \$5 million. The Common shares are owned by a Family Trust.
- Father is concerned that the trust assets have greater value than his own personal assets. Father receives a salary for managing the real estate calculated as a standard management fee of 3%. He wishes to increase this to 4%. A third-party manager would charge 3%.
- As solicitor for Father, Holdco and Family Trust, what advice do you give Father?
- What are your duties as a Director of Holdco?
- What are your duties as Trustee of the Family Trust?



Bonuses, Management Fees, Salary

- *Armitage v. Nurse*¹¹ involved a complex series of trusts. Under the terms of a variation of the trust, the property in a marriage settlement was partitioned between Paula Armitage and her mother. Part of the land was transferred to Paula's mother; the remainder of the land was allocated to a trust for Paula.
- Paula complained that the trustee had appointed a company to manage Paula's land. The sole directors and shareholders of the company were Paula's mother and grandmother.
- Paula claimed that this was not only imprudent, but forbidden, because the settlement provided that no income or capital should be paid to or applied beneficially for Paula's mother or grandmother.
- She also alleged that the trustees had failed to properly supervise the company in its management of the property in Paula's trust.

¹¹ [1998] Ch. 241



- Millett, L.J. stated as follows:

It is the duty of a trustee to manage the trust property and deal with it in the interests of the beneficiaries. If he acts in a way which he does not honestly believe is in their interests then he is acting dishonestly. It does not matter whether he stands or thinks he stands to gain personally from his actions. A trustee who acts with the intention of benefiting persons who are not the objects of the trust is not the less dishonest because he does not intend to benefit himself.¹²

- In this instance, the trustee engaged a company owned by a parent and grandparent to manage the trust property, even though the mother and grandmother were performing no services directly, but, rather, were profiting as a consequence of the management agreement.

¹² [1998] C.H. 241



Illustration on Bonuses

- Entrepreneur has redeemed all his preference shares in a frozen Opco.
- As a director, you are asked to approve a bonus for an entrepreneur to eradicate the extravagant “shareholder loans” booked for drawings and personal benefits.
- You become aware that the entrepreneur has Sugar Babe on the payroll for interior decorating services.
- You are asked to authorize a guarantee of a bank loan for Sugar Babe Interior Decorating.
- Is there privilege attached to any of this information? You learned this as a director, not as a lawyer.
- What is your obligation as a Trustee of the Family Trust that owns the shares?



Limitation Period

- If any loss arises to the corporation as a result of these actions, the corporation may lose its right to make a claim against the directors or any third party, including the law firm, if a limitation period intervenes.
- This would leave the trust beneficiaries with a cause of action against the Trustees and the law firm.



Power to Borrow

- It is the directors who have the ability to borrow funds on behalf of the corporation. Corporate borrowings may reduce or impair the value of the estate or trust assets depending on the use of the borrowed funds. Certain corporate activity might result in the diminution of value of the shares which comprise the estate or trust property.



Power to Guarantee

- The directors have the ability to guarantee on behalf of the corporation.
- This is perhaps one of the most difficult and challenging decisions to make. A profitable corporation may be asked to guarantee the obligations of an affiliate, which involves high risk activity.
- Where the shareholders of the guaranteeing company and the borrowing company are the same, this does not pose a conflict.
- However, where the shareholders of the borrower are different from the shareholders of the guarantor, this represents a problem.



Illustration re Guarantees

- Father has incorporated Newco to enter into a development project. He is the sole shareholder of Newco. The upside is significant, but it also involves significant risk.
- The bank requests that Father give a guarantee and pledge his preference shares of Holdco.
- The bank also requests that Holdco give a guarantee and provide collateral security against the underlying assets of Holdco.
- As a director of Holdco and Trustee of the Family Trust which owns the common shares of Holdco, what conflicts do you perceive?



The Benefit of the Family versus the Benefit of the Beneficiaries

- In *Walker v Stones*,¹³ a law firm acted for both a father and his company. A partner was a Trustee of a family trust (the “Bacchus Trust”) and another “occasional” partner was a director of the subsidiary corporation of the Bacchus Trust.
- The Trustees of the Bacchus Trust subscribed for bonds issued by father’s company. The bonds become worthless. The trust assets were completely eroded.

¹³*Walker v. Stones* [2001] QB 902



Indirect Benefit

“Amongst those stated reasons are the asserted facts that Mr. Walker’s children (indirectly) had a substantial interest in Birdcage Walk, which was said to hold about 24.7% of the issued ordinary shares of BWG; that another of Birdcage Walk’s assets was a debt of about £4.4 M owed to it by Mr. Walker and that his ability to repay it was likely to depend on the financial circumstances of BWG; and that **the prosperity of Mr. Walker’s children and their families was . . . dependent on the survival of BWG and hence on the success of the bond issue**”.



Indirect Benefit

- ...The suggested inference that, throughout all the many transactions of 1990 and 1991, Mr. Stones consistently and consciously used his position as trustee to further or protect the financial interests of BWG, Birdcage Walk and Mr. Walker, by deliberately sacrificing the financial interests of the Bacchus trust beneficiaries, derives support from an examination of the circumstances in which... very substantial amounts of money belonging to [the Trust subsidiaries] came to be wrongfully diverted from those companies, with the assistance or at least the acquiescence of Mr. Stones.



Fraud Upon a Power

- Is a “family benefit” a fraud upon a power?
- Does this contribute “dishonest behaviour” within the LawPro exclusions?



Dishonest Breach of Trust

“Then it is suggested that the pleading is equivocal because, even if Mr. Stones sought to benefit Mr. Walker or his two companies in such manner as he knew and intended would be detrimental to the financial interests of the beneficiaries, this would not necessarily import “dishonesty” on his part, within the meaning ascribed to the phrase in *Armitage v Nurse* or within clause 15 of the Bacchus Trust deed. The answer to this point is in my judgment to be found in a short passage from Millett LJ’s judgment in *Armitage v Nurse* [1998] Ch 241, 251F quoted above: **“A trustee who acts with the intention of benefiting persons who are not objects of the trust is not the less dishonest because he does not intend to benefit himself.”** I infer from this sentence that Millett LJ would have held that a trustee who acts with the specific intention of benefiting persons whom he knows not to be objects of the trust, in the knowledge that this will be at the expense of the financial interests of the beneficiaries, cannot invoke a trustee exemption clause, such as clause 15 of the Bacchus trust deed, however “pure and honest he considers his motives to be”; the protection which may be afforded to another trustee who commits a “judicious” breach of trust will never be available to him. If this be so, I would agree. **Applying the objective test referred to above, no reasonable solicitor-trustee would regard such a course as honest.”**



Dishonest Breach of Trust

- In my judgment the plaintiffs have on the pleadings and evidence shown sufficient foundation for **a case against Mr. Stones based on dishonesty** in the sense explained above, even though it is not suggested that he personally stood to gain from any of the relevant transactions.



The Solicitor Standard of Care

“With respect, however, I find myself unable to agree with the third proposition, if stated without qualification. At least in the case of a solicitor-trustee, a qualification must in my opinion be necessary to take account of the case where the trustee’s so-called “honest belief”, though actually held, is so unreasonable that, by any objective standard, no reasonable solicitor-trustee could have thought that what he did or agreed to do was for the benefit of the beneficiaries. I limit this proposition to the case of a solicitor-trustee, first, because on the facts before us we are concerned only with solicitor-trustees and, secondly, because I accept that the test of honesty may vary from case to case, depending on, among other things, the role and calling of the trustee: compare *Twinsectra Ltd v. Yardley* [1991] Lloyd’s Rep Bank 438, 464 per Potter LJ. In that case, the court regarded the standard of honesty applicable in the case of the defendant solicitor, Mr. Leach, as being “**that to be expected of a reasonably prudent and honest solicitor**”.”



SCC Conflicts Cases for Lawyers

- *McDonald Estate v Martin*, 1990 3 SCR 1235
- *R v Neil*, 2002 SCC 70
- *Côté v Rancourt*, 2004 SCC 58
- *Celanese Canada Inc v Murray Demolition Corp*, 2006 SCC 36
- *Strother v 3464920 Canada Inc* 2007 SCC 24
- *Galambos v Perez*, 2009 SCC 48
- *Canadian National Railway Co v McKercher LLP*, 2013 SCC 39



Law Societies

- The Federation of Law Societies of Canada
- *Barreau du Québec*
- Law Society of Alberta
- Law Society of British Columbia
- Law Society of Manitoba
- Law Society of New Brunswick
- Law Society of Newfoundland and Labrador
- Law Society of the Northwest Territories
- Law Society of Nunavut
- Law Society of Prince Edward Island
- Law Society of Saskatchewan
- Law Society of Upper Canada
- Law Society of Yukon
- Nova Scotia Barristers' Society



QUESTIONS???



THANK YOU!!!