

THE COMMONS INSTITUTE

Ethical Considerations in the Practice of Real Estate Law

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Ethics and Client Cash Flow:
Trust Account Management

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The day of a real estate closing involves many moving parts, and the movement of closing funds is only one of many components of a closing. However, the movement of closing funds by a real estate lawyer through the firm's trust account is one of the riskiest obligations law firms face. To assist practitioners in determining what makes sense for his or her practice, this paper will examine the pros and cons of wire transfers, tips to confirm that a bank draft or certified cheque is legitimate, the Law Society of Upper Canada's ("LSUC") requirements for the payment of land transfer tax and registration fees, and a review of LAWPRO's trust account coverage.

PAYMENT SYSTEMS IN CANADA

As part of the examination of the movement of funds through a trust account, it is important to review some payment concepts and the entities that manage our payment systems. The Bank of Canada works closely with the Canadian Payments Association (CPA), which was established by statute in 1980.² The CPA is the not-for-profit organization that operates the Automated Clearing Settlement System and the Large Value Transfer System. These two systems "move" money in Canada.

AUTOMATED CLEARING SETTLEMENT SYSTEM VS. LARGE VALUE TRANSFER SYSTEM

ACSS

The Automated Clearing Settlement System ("ACSS") handles the vast majority of payments in Canada, and encompasses the movement of funds in every way *except* wire transfers (i.e. everything from traditional paper-based

¹ The research contribution of Manali Tasha Pradhan, student-at-law, is acknowledged and appreciated.

² "Who We Are" and "What We Do", online: Canadian Payments Association <<https://www.cdnpay.ca/imis15/eng/About.aspx>>. [CPA].

cheques to electronic transactions such as debit card payments). Specifically, bank drafts and certified cheques are cleared and settled through ACSS.

Through ACSS, payments are exchanged throughout the business day. The settlement of payments through ACSS takes place through six regional settlement points across Canada for paper items, and one national settlement point for electronic transactions.³

At these settlement points, paper based payments are sorted by computerized readers and electronic payments are redirected to the data centre of the applicable direct “clearer” in the same region. The direct “clearer” enters the payment information into its ACSS terminal, and the next business day, payment instruments are returned or electronically delivered to the institutions upon which they are drawn.⁴ Along the way, the appropriate debits, credits and adjustments are made to reflect the movement of the payment instrument.⁵

Pros & Cons of ACSS

To determine which method of moving funds is most appropriate in a given circumstance, consider the following pros and cons of ACSS:

PROS

Common Practice

Moving funds by way of certified cheque or bank draft in respect of real estate transactions remains the most common method of moving closing funds (especially in residential real estate transactions).

Efficient Practice

The process of delivering funds by way of a direct deposit into the Vendor’s solicitor’s trust account (with a copy of the certified cheque or bank draft and the deposit slip being circulated by fax or e-mail) is a quick and streamlined way to move funds on the day of closing.

CONS

Incidence of Fraud

Fraudsters are becoming increasingly sophisticated, and fraudulent instruments are becoming harder to detect.

³ “Automated Clearing Settlement System”, CPA, *ibid* at <http://www.cdnpay.ca/imis15/eng/Clearing_Settlement/Automated_Clearing_Settlement_System/eng/sys/Automated_Clearing_Settlement_System.aspx?hkey=1edb79e1-3b3a-48f1-b71e-f14786a58bc5>.

⁴ *Ibid*.

⁵ Canada’s Major Payments Systems, *Large Value Transfer System (LVTS)* and *The Automated Clearing Settlement System (ACSS)*, online: The Bank of Canada <<http://www.bankofcanada.ca/core-functions/financial-system/oversight-designated-clearing-settlement-systems/canadas-major-payments-systems/>>.

Delay in Clearing

Even though a credit may appear in your trust account, if the payment was made through ACSS, it is not necessarily “cleared”. Generally, it takes up to three business days for a paper payment instrument to work its way back to the issuing financial institution where the decision is made whether the payment will be honoured. If the payment cannot be honoured (e.g. a stop payment on a cheque), it can take up to an additional three business days for the instrument to be returned to the financial institution that accepted the instrument for payment. Payments by way of certified cheques and bank drafts do not become final and irrevocable until the next business day at the earliest.⁶

Up to Six Years for the Payment to Truly be Considered “Final”

Bank drafts and certified cheques are subject to return in two cases under the CPA clearing rules. In the case that the negotiable instrument was materially altered after it was issued (i.e. a change to the amount or the payee), for up to 90 days following receipt by the drawee financial institution.⁷ A cheque of any type (whether certified or not) with a forged endorsement can be returned up to *six years later*.⁸

Posting Delays

Some banks maintain policies whereby they will not post electronic funds transfers received through ACSS to a beneficiary’s account until the next business day, and possibly longer where the other institution is not within the same region, or not one of the major financial institutions. Check in with your bank to determine its policy.

LVTS

The Large Value Transfer System (LVTS) was launched on February 4, 1999. It was designed and is operated by the CPA. The Bank of Canada is intimately involved with and oversees the LVTS.⁹ Currently, all Canadian dollar wire transfers are made through the LVTS.¹⁰ Despite the connotation that the sums moved through the system are “large value”, there is no minimum amount of funds that may be transferred.

⁶ “Cheque Clearing”, CPA, *supra* note 2 at <http://www.cdnpay.ca/imis15/eng/FAQs/Cheque_Clearing/eng/faq/Cheque_Clearing.aspx#bm05>. Also See “What is LVTS v. ACSS & Why Should You Care?”, *LawPro Magazine: Practicing Law in an E-World* (December 2004) 12, online: <<http://www.practicepro.ca/LawPROmag/FundsHandling.pdf>>.
⁷ “Show me the Money”, *LawPro Magazine: PracticePro: 10 Years of Helping Lawyers* (Summer 2008) 6, online: <http://www.practicepro.ca/LawPROmag/Wire_Transfer_Benefits.pdf>.

⁸ *Ibid.*

⁹ Neville Arjani and Darcey McVanel, “A Primer on Canada’s Large Value Transfer System” *Large Value Transfer System* (1 March 2006) online: Bank of Canada <http://www.bankofcanada.ca/wpcontent/uploads/2010/05/lvts_neville.pdf> at 7.

¹⁰ *Ibid.*

It is important to note that inter-branch transfers or automated funds transfers between banks are cleared through ACSS. Even though they may be described as a wire, they do not pass through LVTS, so make the appropriate inquiry to determine which system funds will be moved through if the process is described as a wire.¹¹

Pros & Cons of LVTS

To determine which method of moving funds is most appropriate in a given circumstance, consider the following pros and cons of ACSS:

PROS

Guaranteed Funds

All funds transfers through LVTS are final, can not be pulled back, dishonoured or unwound, and the funds are guaranteed. The CPA boasts that “immediate intraday finality is achieved because settlement of the LVTS is guaranteed under all circumstances.”¹² This guarantee can be made because the financial institutions which are members of the LVTS pledge specified amounts of collateral as security for the funds that they are moving, and the system is also supported by a guarantee by the Bank of Canada.¹³ The risk of receiving fraudulent funds is eliminated when using the LVTS.

Paperless Movement of Funds

Wire transfers eliminate the need to deliver and review physical negotiable instruments. Money is moving electronically, thus possibly reducing courier costs and delays with physical delivery (i.e. the avoidance of line-ups at your bank where wires can be initiated from your office, delays due to inclement weather, traffic, courier issues).

Recommended Method of Moving Funds

Wires are recommended by the LSUC and LAWPRO.

CONS

Afternoon “Cut-Off Times”

Some banks have policies of “wire cut-off” deadlines in the early or mid-afternoon, and similarly, the CPA’s LVTS Rule 10 provides that where transfers received within three hours of the end of the business day of the bank branch may not be made available until the branch opens the next business day.

¹¹ E&O Insurance: Lawyers in Private Practice FAQs, *About LawPRO’s enhanced coverage for counterfeit certified cheques and bank drafts*, online: LawPro

<https://www.lawpro.ca/insurance/pdf/FAQs_enhanced_fraud_coverage2.pdf> at question 22.

¹² *Supra* note 9 at 5.

¹³ *Ibid.*

Not “Instant”

Despite the claim that funds are transferred quickly through the LVTS, many practitioners have shared stories of a wire gone “missing” for several hours. There are several “steps” that constitute a wire transfer, and a delay at any one of the “steps” can be out of the control of both the law firm and its own bank. However, after the sending financial institution initiates the wire, the CPA can complete the wire transfer to the receiving institution in one minute.¹⁴ With time and experience, the speed of a LVTS wire has improved.

Customarily Higher Costs

Anecdotal evidence is that the cost of a bank draft or certifying a cheque is often less than the cost to send wire transfers. Some financial institutions also charge both a sending and receiving fee. Speak to your bank about these fees.

TIPS TO CONFIRM THAT A BANK DRAFT OR CERTIFIED CHEQUE IS LEGITIMATE

File Opening Red Flags

If you decide to accept certified cheques or bank drafts during the course of a transaction, LAWPRO has advised to be wary of the following potential red flags at the initial stages and during the progress of a matter:¹⁵

- (a) The initial contact email is generically addressed and Bcc'd to many people;
- (b) The name or email address of the email sender is different from the name or email address of the person the lawyer is asked to reply to in the body of the email or the person identified in the signature line;
- (c) The client uses a free email service (such as Gmail, Hotmail or Yahoo) even where the matter is on behalf of a business entity;
- (d) The domain name used in the personalized email address or website was recently registered (use the site <http://www.whoisxmlapi.com/> to see when a website was registered);
- (e) The IP address of the email indicates that the sender's geographic address does not coincide with where they claim to be located;
- (f) The client is new to your firm or is from a distant jurisdiction;

¹⁴ *Supra* note 7.

¹⁵ LawPro, News Release, “Fraud Fact Sheet: Bad Cheque Scams” (2012), online: <<http://www.practicepro.ca/practice/pdf/fraudinfosheet.pdf>> at p 2.

- (g) The client insists on completing the matter close to a banking holiday;
- (h) The client is in a rush – and pressures you to “get the deal done quickly”;
- (i) The client and others involved are not concerned if short-cuts are taken;
- (j) The cheque is drawn from the account of an entity that appears to be unrelated and/or the payment of the net proceeds is going to a third party who appears unrelated to the matter;
- (k) The amounts involved are different than expected or change without explanation; or
- (l) The client asks for an urgent movement of funds based on an unexpected change of circumstances.

How to Detect a Fraudulent Cheque

The following are some tips to help you spot a fraudulent certified cheque or bank draft:

1. Inspect the security features on the cheque:

- Most cheques, money orders and bank drafts issued by Canadian banks have built-in security features. The features include but are not limited to: watermarks and intricate designs that disappear when a cheque is scanned or photocopied.¹⁶
- Details about these built-in security features usually appear on the back of the cheque/draft.

2. Know your client:

- The recipient of a cheque should familiarize themselves with the person or entity issuing the cheque.
- In any event, lawyers should follow client identification and verification rules as required by sections 22 and 23 of By-Law 7.1 of the *Law Society Act*.¹⁷

3. Verify referrals from other professionals:

- Where a client has been “referred” to a lawyer by another professional, verify the referral by contacting the person who provided the

¹⁶ Canadian Bankers Association, Newsletter, “Fraud Prevention Tip of the Month” (June 2007).

¹⁷ RSO 1990, Chapter L8.

reference.

- Where an unknown lawyer makes a referral, check the LSUC's database of lawyers to ensure that the individual is licensed. Compare the information in your possession with the information on the LSUC's website.¹⁸

4. Carefully check the payor's information with an independent third party.

- The use of contact information provided by the potential fraudster to contact the payor or the payor's bank is not advised.¹⁹
- Instead, to verify information, use telephone books, the internet and other resources to cross-check names, addresses and telephone numbers to see if they correspond to the information provided.²⁰
- Do reverse searches on phone numbers.²¹
- Look up addresses using Street View on Google Maps.²²
- Fraudsters often create phony law firm websites. Ensure that the law firm and lawyer to whom the funds are being transferred are legitimate by comparing their information using independent source documents, data or information.
- Where the transaction involves real property, also use the title search to cross-check.²³ Do the addresses for service match? If you are dealing with a corporation, does the corporate profile match? Are there "new" signing officers involved?

5. Call or visit the bank on which the instrument was written.

- A bank has internal processes in place to verify the authenticity of their cheques, and is in a better position to determine the legitimacy of a certified cheque or bank draft.
- Ensure that the cheque or draft contains an authorized signature.²⁴
- Ensure that the issuer of the cheque is as expected – for instance, that

¹⁸ Law Society of British Columbia, Newsletter, "Bad Cheque Scam: Steps to manage the risk" (2014).

¹⁹ U.S. Department of the Treasury: Office of the Comptroller of the Currency, Consumer Advisory, CA 2007-1, "Avoiding Cashier's Check Fraud" (January 16, 2007).

²⁰ *Supra*, note 15.

²¹ *Ibid.*

²² *Ibid.*

²³ *Supra*, note 18.

²⁴ "Definition of Certified Cheque", online: Investopedia Dictionary <<http://www.investopedia.com/terms.asp>>.

the expected person or entity is named as the drawer of a cheque.²⁵

- When following up with a bank, do not use the telephone number or other contact information provided on the instrument, as that information is likely associated with the fraudster.²⁶ Obtain the contact information for the bank from an independent source.

6. The cheque can also be verified at your primary bank.

- Ask your own bank branch to help. Your branch can contact the bank on which the instrument was drawn and attempt to verify the authenticity of the cheque.
- Have the bank confirm in writing that the funds from the deposit are safe to withdraw.²⁷

7. Ensure the cheque, money order or bank draft has cleared and the money has been confirmed prior to releasing any funds.

- Understanding the difference between “funds being available for withdrawal from the account” and “a cheque having finally cleared in your account” is essential.²⁸
- Cheques are generally subject to a “holding period”, wherein a cheque is held until the funds are verified as sufficient, at which time the funds are released to the recipient.
- Accordingly, a cheque that purports to be drawn on an actual bank account may be posted to your account initially, with the bank later discovering that the instrument was fraudulent.
- The holding period for Canadian banks is generally six days, whereas the holding period for international banks is longer.²⁹ Talk to your bank about its policy.

8. Contact the entity making the payment to verify that they are aware of the payment, and the receiving entity to confirm that it is expecting a payment.³⁰

9. The Trust Payment Protocol

- LAWPRO suggests that in respect of trust account outflows, lawyers

²⁵ *Supra*, note 18.

²⁶ *Supra*, note 19.

²⁷ *Supra*, note 15.

²⁸ *Supra*, note 19.

²⁹ *Supra*, note 16.

³⁰ *Supra*, note 15.

should implement a policy of always contacting the bank in circumstances where the client has not been with the Firm for more than six months, and has not paid at least two firm invoices.³¹

- LAWPRO also suggests that lawyers should adopt a policy requiring that funds deposited in their account by a wire through LVTS.³²
- Clients should never be allowed to directly deposit a cheque or a bank draft into the trust account if the funds need to be moved out within a few business days. Insist on physically handling the payment instrument.

10. Other general tips include:

- Ensuring that the cheque is properly dated, completed, and does not show any signs of alteration;
- Enacting a policy of not accepting post-dated cheques or cheques made out to the another party and endorsed over to your firm;
- Do not accept cheques for an amount greater than the balance due on closing. A common scam involves receipt by the lawyer of a larger amount of funds than necessary, and the fraudster later asking the lawyer to return the difference.³³ By the time the initial fraudulent cheque is discovered, the fraudster has cashed in the cheque sent to him or her by the lawyer.
- Enact a policy of not accepting counter cheques (cheques with no preprinted information such as a name, address, or account number).
- Always maintain a paper trail that effectively details the whole transaction, in accordance with your obligations under the LSUC's By-Law 9.

³¹ *Supra*, note 18.

³² "Keep Your Guard Up! More Sophisticated Cheque Scams Targeting Lawyers", *LawPro Magazine: 2009 in Review* (May/June 2010) 22, online: <<http://www.practicepro.ca/LawPROmag/KeepYourGuardUp.pdf>>.

³³ *Supra*, note 19.

LAW SOCIETY OF UPPER CANADA'S BY-LAW 9

Available at:

[http://www.lsuc.on.ca/
WorkArea/DownloadA
sset.aspx?id=214748502](http://www.lsuc.on.ca/WorkArea/DownloadAsset.aspx?id=214748502)

⁴ The LSUC details a lawyer's obligation as it relates to trust funds in its By-Law 9.³⁴ By-Law 9 is entitled "Financial Transactions and Records", and should be reviewed by both lawyers and their bookkeepers.

Part IV of By-Law 9 governs the establishment, use, and closing of trust accounts. Section 7(5) of By-Law 9 allows a lawyer to maintain one or more trust accounts. There are four types of trust accounts³⁵:

1. Mixed Trust Accounts.

- The most common type of trust account, where funds held in trust for multiple clients are deposited.
- The interest earned on your mixed trust account must be paid to the Law Foundation of Ontario in accordance with Section 57(1) of the *Law Society Act*.³⁶

2. Interest Bearing Trust Accounts.

- These accounts are used where a law firm holds a large sum of money in trust for a client for long periods of time, which bear interest for the benefit of the client.
- An interest bearing trust account can only hold funds on behalf of one client, otherwise it is considered a mixed trust account, and the interest must be paid to the Law Foundation of Ontario in accordance with Section 57(1) of the *Law Society Act*.³⁷

3. Estate and Power of Attorney Trust Accounts.

- This type of trust account may be used where you are exercising a power of attorney or have sole signing authority over estate assets.

³⁴ Law Society of Upper Canada, by-law No 9, *Financial Transactions and Record*, (3 May 2011).

³⁵ Manage Your Practice, *How to Open and Operate a Trust Account*, online: The Law Society of Upper Canada <<http://www.lsuc.on.ca/For-Lawyers/Manage-Your-Practice/Financial-Management/Billing/Collections/Trust-Accounts/How-to-Open-and-Operate-a-Trust-Account/>>.

³⁶ *Supra* note 17.

³⁷ *Ibid.*

4. Electronic Registration Mixed Trust Account.

- This type of trust account is a mixed trust account used by real estate lawyers to pay land transfer tax and registration fees, and are also known as your electronic registration bank account (“ERBA”).
- Note that your ERBA does not need to be a trust account; it may also be a general account.
- The electronic registration mixed trust account is examined more thoroughly below.
- Client funds may only be kept in your trust ERBA for a maximum of five days.
- Any interest earned in your electronic registration mixed trust account must be paid to the Law Foundation of Ontario in accordance with Section 57(1) of the *Law Society Act*.³⁸

Trust Accounting Tips

INVESTING
FUNDS ON
BEHALF OF A
CLIENT

A noteworthy requirement relating to investments made on behalf of a client should be kept in mind if you hold large deposits for a long period of time. It is common practice to “invest” funds being held for long periods of time in your mixed trust account (i.e. deposits under purchase agreements). Section 8(1)(a) of By-Law 9 sets out requirements lawyers must follow in these circumstances. Before making the investment, the lawyer must explain and be satisfied that his or her client understands:

1. How the investment pays income;
2. The nature of the risk associated with the investment; and
3. Whether there will be sufficient funds available when the client needs them to be available (e.g. can you break the investment in time for closing).³⁹

After confirming that your client understands and agrees with the above, you must receive your client’s written instructions to make the investment, or confirm verbal instructions in writing (to ensure you aren’t unintentionally providing financial advice).⁴⁰ When you invest funds on behalf of a party, you should obtain that

³⁸ *Ibid.*

³⁹ *Supra* note 35.

⁴⁰ *Supra* note 34 at s 8(1)(a).

party's social insurance number (if an individual) or its corporation number or business number (if not an individual) for income tax purposes prior to making the investment. After year-end, you will receive a T5 supplementary income slip from your bank to identify the interest earned on the investment, and you must then issue T5 slips to the recipient of the interest.⁴¹

**USE OF
TRUST
ACCOUNTS**

A final note on trust accounts generally. Remember that funds moving through your trust account must be for purposes related to the provision of legal services. Do not use your trust account for the deposit of any funds not held in your capacity as a lawyer or paralegal.⁴²

LSUC REQUIREMENTS FOR THE PAYMENT OF LAND TRANSFER TAX AND REGISTRATION FEES

Your Electronic Registration Bank Account

Your Teraview licence agreement includes a requirement to maintain an electronic registration bank account (“ERBA”). The ERBA is the account from which Teranet is authorized to debit registration fees and payments of land transfer tax (LTT). You may use either a trust account or a general account as an ERBA. Each time you submit an instrument for registration, it is deemed to be an authorization for Teranet to withdraw the applicable LTT and registration fees and from your ERBA. Your ERBA cannot be the same bank account as your existing mixed trust account.⁴³

Prior to closing, it is usual practice that your purchaser client is provided with a figure required to close a transaction, which will include any balance due on closing, applicable LTT and registrations fees, and any disbursements due to be paid on closing (i.e. title insurance premiums), less any funds you are receiving from a financing. Depending on the type of ERBA you maintain, different logistics apply to the payment of LTT and registration fees from this amount.

**TRUST
ACCOUNT
ERBA**

If using a Trust ERBA, once the law firm receives the closing funds, it must deposit the entire amount received from the client into its mixed trust account (unless the client delivers a separate cheque representing the applicable LTT and registration fees). A trust cheque from the mixed trust account must then be drawn in the amount of the LTT and registration fees, and then deposited into the firm's ERBA. Funds may be located in a Trust ERBA for a maximum of 5 days.⁴⁴

⁴¹ *Supra* note 35.

⁴² Practice Management Topics, *Trust Account Operation*, online: The Law Society of Upper Canada <www.lsuc.on.ca/TrustAccountOperation/>.

⁴³ “Payment of Land Transfer Tax and Registration Fees” (6 March 2001), online: Law Society of Upper Canada <[⁴⁴ *Supra* note 34.](http://www.lsuc.on.ca/For-Lawyers/Manage-Your-Practice/Practice-Area/Real-Estate-Law/Payment-of-Registration-Fees-and-Land-Transfer-Tax-(March-6,-2001)/>.</p></div><div data-bbox=)

The LSUC Form 9B (entitled Authorization of Withdrawal by Teranet) must be completed, signed, and submitted upon the occurrence of registration in Teranet. The Teranet confirmation (called the docket tax/fee summary in the Teranet system) is compared with Form 9B no later than 5pm on the next business day following the registration. As required by Section 18(8) of By-Law 9, a Trust ERBA must be reconciled and included in your usual monthly trust comparison.⁴⁵

If you are completing a registration unrelated to a closing, where you have not collected an amount from your client prior to submitting a registration, the proper procedure is: 1. to issue a “loan” to your client for the registration fees from your general account, 2. deposit the amount required into your trust ERBA, and 3. charge the client for the disbursement in the usual course.

**GENERAL
ACCOUNT
ERBA**

In the scenario where a general account is used as your ERBA, the funds received from a client representing the total closing costs (i.e. balance due on closing, LTT, registration fees and disbursements) are to be deposited into your trust account. Following registration, Teranet is authorized to debit your ERBA general account. Only after registration may funds be moved by way of trust cheque from your trust account for deposit into your general account to reimburse the general account. The LSUC allows for a single trust cheque to be drawn to reimburse your ERBA general account if you are closing multiple transactions in one day.⁴⁶

LAWPRO'S TRUST ACCOUNT COVERAGE

LAWPRO's base premium has remained at \$3,350 since 2011 and will remain at the same rate for 2015. The insurer sees annual claim costs of almost \$100 million.⁴⁷

COVERAGE

Under LAWPRO's standard E & O insurance, you are covered for claims brought against you (as defined in the policy) relating to your provision of professional services up to a maximum of \$1 million per claim/\$2 million in the aggregate. The standard deductible is \$5,000.⁴⁸ If client funds are lost due to your handling of a fraudulent payment instrument, you are covered from claims by clients up to these maximum amounts.

**ENHANCED
COVERAGE**

In 2010, LAWPRO added enhanced coverage (Endorsement No. 7) for counterfeit certified cheques and bank drafts. The existing standard E & O insurance coverage did not protect your trust account if a fraudulent disbursement of funds resulted in an overdraft in your trust account, or where there were no client funds lost. It only covered claims arising out of the circumstance where other client's funds were lost; but

⁴⁵ Ibid note 34 at s 18(8).

⁴⁶ Ibid at p 5.

⁴⁷ “2015: Fifth Year of Premium Stability”, *Law Pro Magazine: Insurance Issue* 13.3 (October 2014) 1, online: <http://www.practicepro.ca/lawpromag/LawPROmagazine13_03_Oct2014.pdf>.

⁴⁸ E&O Insurance, *Insurance Type: Standard Program*, online: LawPro <http://www.lawpro.ca/insurance/private_practice.asp?section=IT#base_program>.

where your trust account went into a negative balance, that negative balance was not covered under the former coverage.

The logic is that generally, LAWPRO's coverage covers legitimate client funds and client losses related to a lawyer's performance of professional services. An overdraft is not damage to a client. It is damage to the law firm. LAWPRO clarifies that "the claim of the bank is for payment of a debt based on contract, not for damages arising out of the performance of professional services- which is the basis on which coverage is generally provided under a professional liability insurance policy".⁴⁹

The 2010 enhanced coverage of Endorsement No. 7 added some coverage where that overdraft resulted from a lawyer's handling of a counterfeit certified cheque or bank draft.⁵⁰ This coverage is provided by LAWPRO at no extra cost over the base premium. The enhanced coverage is subject to a sublimit of \$500,000 per claim in the aggregate per firm per year, inclusive of claim expenses, indemnity payments and costs of reimbursing your account. The coverage does not apply to retainer deposits, funds representing unearned fees or amounts relating to legal fees, accounts or fee arrangements, and deductible.⁵¹ The coverage comes with some requirements imposed on the law firm when dealing with certified cheques or bank drafts that must be met for the coverage to apply, as follows:

**1. DETERMINE
THE FUNDS
ARE
AVAILABLE**

EITHER:

1. **A)** You must wait at least eight business days following the deposit of the negotiable instrument into your trust account before disbursing the funds;

OR

1. **B)** You must receive written confirmation from either your bank or the drawee bank stating that either bank/financial institution has verified the validity and legitimacy of the certified cheque or bank draft. The written confirmation need not take any specific form, but should confirm that the Canadian financial institution named as drawee on the negotiable instrument has verified the validity of the same and that it is safe to withdraw the funds from deposit⁵². Also include the date the confirmation was given, the name of the person who provided the confirmation, the type of negotiable instrument and number, name of the drawee, and the dollar amount, along with your client's name, and file name and the number. It cannot be a memo in your file. The written confirmation must be sent or received by your firm. If the drawee bank agrees to provide verbal confirmation of the negotiable instrument, but refuses to provide that confirmation in writing, you can send your written confirmation of that

⁴⁹ *Supra* note 11.

⁵⁰ *Ibid.*

⁵¹ *Ibid* at question 4.

⁵² *Ibid* at question 12.

conversation to the attention of whomever provided you with the verbal confirmation.
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AND

**2. INSPECT
THE
CANADIAN
PAYMENT
INSTRUMENT**

2. The certified cheque or bank draft must be a Canadian financial institution, and the certified cheque or bank draft must have been physically inspected and deposited by the lawyer or a partner or employee of your firm.

This enhanced coverage also applies to funds you are receiving from a lender. If you aim to meet the requirements of the enhanced coverage, you may have to require, for example, that your residential purchaser/borrower clients advise you well in advance of who their lender will be, so that you can ensure the method of delivery of the funds will allow you to comply with the requirements (i.e. you will have to physically inspect the negotiable instrument).

Remember that the original, existing coverage does cover the loss of legitimate client funds in the case of a fraudulent instrument passing through your account, without any special requirements needing to be met (up to the policy limit). However, for coverage for an overdraft to apply, the requirements above must be met. As is always the case, you will have to consider the risks and impact on your practice and determine the best approach for your practice.

Alternatively, funds could be wired through LVTS, which eliminates the risk of handling counterfeit funds. If you decide this makes sense in your practice, consider setting out the requirement in your retainer letter that all funds must be delivered by wire transfer through LVTS.

**IN ANY EVENT, IF YOU SUSPECT YOU ARE INVOLVED IN A FRAUD,
CALL LAWPRO AT 1-800-410-1013 OR 416-598-5899.**

⁵³ *Ibid* at question 11.