No. 04/01

Misappropriation of funds by unauthorized transfers from trust

John Taylor Martin

Vancouver, BC
Called to the bar: May 10, 1977
Resigned membership: October 15, 2003

AND

Craig Kiyokata Iwata

Vancouver, BC
Called to the bar: July 10, 1980
Undertook to cease practice: October 15, 2003
Became non-practising member: December 17, 2003
Resigned membership: May 6, 2004

From 1995 to 2003 Mr. Martin and Mr. Iwata were partners in the firm of Martin & Associates in Vancouver.

The B Bank misappropriations

Mr. Martin and Mr. Iwata were signatories on their law firm's trust account and general account at B Bank. On 16 occasions between September, 2001 and February, 2003, Mr. Martin and Mr. Iwata withdrew funds from the firm's trust account at B Bank and deposited these funds to the firm's general account. They made these withdrawals even though they knew that the funds were not the property of their firm but were in trust for clients of the firm. They withdrew the funds from trust for deposit to their general account to ensure there were sufficient funds in that account to cover certain cheques. The firm had no overdraft protection on its general account at B Bank. Each time after the funds were withdrawn from trust and deposited to the firm's general account, Mr. Martin and Mr. Iwata (later that same day or the following day) transferred funds from the general account back to the trust account in order to replenish the trust account and repay the funds taken.

The H Bank misappropriations

Martin and Associates also held a trust account and general account at H Bank. Mr. Martin and Mr. Iwata were signatories on these accounts.

The firm's general account at H Bank operated as a line of credit, with a credit limit of $265,000.

It was the practice of H Bank's account manager to check the firm's indebtedness on the line of credit by 11:00 am each day and determine whether the overdraft was within acceptable limits. Should it not be, the bank's policy would be to permit no further cheques to be covered by overdraft and to require immediate repayment of the line of credit.

Mr. Martin and Mr. Iwata, who knew of H Bank's procedures, instituted a practice of transferring funds from the firm's trust account to its general account to bring the overdraft within acceptable limits. Each morning

before 11:00 am, Mr. Martin or Mr. Iwata, each acting with the full knowledge and agreement of the other, signed a trust cheque, which represented in part trust withdrawals permitted by Law Society Rule 3-56 (for payment of fees) and in part the unauthorized withdrawal of client trust funds. The portion of the cheque that represented an unauthorized withdrawal of funds was recorded in the firm's accounting system separately and reflected a shortage in the trust account. Between March and May, 2003 Mr. Martin and Mr. Iwata made 31 such transfers from the firm's trust account to its general account. In each case, later that day or the following day, Mr. Martin and Iwata arranged for a general account cheque to be deposited into trust to repay the trust shortage.

The reason for these transfers to the general account was to induce H Bank to continue to extend credit to the firm and to refrain from demanding repayment. The client funds withdrawn from trust without authorization were at risk of being removed by H Bank in repayment of the firm's line of credit.

Over the period that Mr. Martin and Mr. Iwata made these transfers, the amount of the transfers increased. They ceased making the transfers after H Bank asked that they do so.

Mr. Martin and Mr. Iwata made unauthorized withdrawals from their firm's trust account at B Bank and H Bank for the purpose of deposit to their firm's general accounts, and subsequently returned the funds to trust. No client of the firm lost any money as a result of these unauthorized transfers.

Trust shortages

Between January, 2001 and September, 2003 Mr. Martin and Mr. Iwata failed on 26 occasions to immediately eliminate trust shortages, contrary to Rule 3-66(1), and failed on 17 occasions to immediately report trust shortages over $2,500, contrary to Rule 3-66(2).

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After the 2002 accountant's report for Martin and Associates revealed exceptions, the Chair of the Discipline Committee ordered an investigation of the firm's books, records and accounts. In September, 2003, following this investigation, Mr. Martin and Mr. Iwata advised the Law Society that they had made transfers from trust to reduce their firm's exposure on its line of credit.

Citations were authorized against Mr. Martin and Mr. Iwata in early October, 2003 and issued in December, 2003. A panel of Benchers was constituted under s. 39 of the *Legal Profession Act* to determine whether to suspend or impose conditions on Mr. Martin and Mr. Iwata pending disposition of the citation. The panel found it was unnecessary to take action, in light of the fact that, on October 15, 2003, Mr. Martin resigned his membership and Mr. Iwata undertook not to practise law pending the disposition of the citation. With consent, a custodian for the firm was subsequently appointed by order of the BC Supreme Court.

In May, 2004, Mr. Martin and Mr. Iwata each admitted to the Discipline Committee that their conduct in withdrawing funds from their firm's trust accounts when they knew the funds were not the property of the firm, but rather were in trust for clients, constituted misappropriation and amounted to professional misconduct and a breach of Rule 3-56. They also admitted to professional misconduct in making transfers from trust to temporarily reduce the firm's line of credit and to induce a bank to continue to extend credit or refrain from making a demand for repayment.

They further admitted to a breach of Rule 3-66 for failure to immediately eliminate trust shortages and failure to immediately report trust shortages over $2,500.

Pursuant to Rule 4-21 the Discipline Committee resolved the outstanding citations against Mr. Martin and

Mr. Iwata by accepting their admissions of professional misconduct and their undertakings:

to refrain from applying for reinstatement to the Law Society for 10 years;

not to apply for membership in any other law society without first advising the Law Society;

not to permit their names to appear on the letterhead of any lawyer or law firm without the written consent of the Law Society;

to obtain written consent from the Law Society before working for any lawyer or law firm in BC.