2010 LSBC 03
Report issued: February 01, 2010
Citation issued: April 18, 2008

The Law Society of British Columbia
In the matter of the *Legal Profession Act*, SBC 1998, c.9
and a hearing concerning

Henry Alexander (Sandy) McCandless

Respondent

Decision of the Hearing Panel on Facts and Verdict

Hearing date: November 16, 17, 18, 19, 2009 and January 14, 2010

Panel: Bruce A. LeRose, QC, Chair, Haydn Acheson, William F.M. Jackson, QC

Counsel for the Law Society: Jaia Rai
Appearing on his own behalf: H.A. (Sandy) McCandless

Background

[1] The citation was issued on April 18, 2008 and amended on October 19, 2009. The citation as amended authorized the Panel to inquire into the following conduct:

1. In the course of your representation of TIC, which participated in an investment scheme through IFC, you engaged in conduct intended to give the shareholders of TIC or some of them the impression that their investment was secure and continuing to generate earnings after you became aware that the B.C. Securities Commission had ordered, among other things, that all persons cease trading in the IFC investment in its Temporary Order and Notice of Hearing dated November 1, 2006 and/or after you became aware that as a result of an investigation by the U.S. Securities and Exchange Commission, a U.S. Court had ordered the appointment of a Receiver over the property and assets of IFC. Your conduct includes but is not limited to the following:

   (a) You failed to inform TIC's shareholders or some of them of the Temporary Order and Notice of Hearing issued by the B.C. Securities Commission and/or the appointment of the Receiver for IFC.

   (b) Through TSC Corp., a company controlled by you, you loaned funds to TIC so that TIC could make regular earnings payments to its shareholders once IFC was no longer in a position to make them, without advising the shareholders or some of them of the true source of their earnings payments.

   (c) [deleted]

2. Through TSC Corp., a company controlled by you, you invested your own funds in IFC through TIC

while you were acting for TIC, placing yourself in a conflict of interest.

3. You accepted funds into your trust account from or on behalf of JC for investment through TIC and then released those funds to DF so that JC would have an interest in the IFC investment scheme in place of DF in circumstances that required you to either

(a) decline to accept, or to return, the funds; or

(b) advise JC of material facts related to the IFC investment known to you, including the fact of allegations being made in B.C. Securities Commission and U.S. Securities and Exchange Commission proceedings and actions taken by these regulators in relation to the IFC investment

but you did not do either.

[2] At the commencement of this hearing, the Respondent admitted that the requirements of Law Society Rule 4-15 regarding issuance and service of the citation had been met.

[3] The citation as amended was entered as Exhibit 3.

[4] The matters set out in the citation were the subject of an Agreed Statement of Facts (" ASF") submitted by both parties and entered as Exhibits 5a through 5d.

[5] Both parties filed extensive documentation.

Facts

[6] In July of 2003 an alleged ponzi scheme operated by IFC was set up in Virginia. IFC was administered by PP and MS.

[7] IFC administered two programs. The second program in time was known both as the Asset Growth Program (" AGP") and often as the MTN program. The MTN program contemplated a minimum capital deposit of $100,000 US to IFC who would leverage those funds to buy " 1st tier medium term bank notes" at a discount and sell the notes for a profit.

[8] Throughout the period from November 17, 2005 until July 4, 2007, the Respondent acted as a lawyer for TIC. On November 17, 2005, on the instructions of CM, the Respondent incorporated TIC. CM was the sole director of TIC at all material times.

[9] TIC was set up to raise $100,000 US by contributions from CM and MMI, a company directed by CM, as well as expected further shareholders including JM and DF. The $100,000 US raised by TIC was to then be invested in the IFC program.

[10] TIC was not the first of the Respondent's clients to invest in the IFC scheme. The ASF establishes that CM was introduced to the scheme by the Respondent.

[11] In 2006 seven persons, both individual and corporate, contributed funds to TIC. These contributors were CM, MMI, DF, JM, HL, GG and TSC Corp. Each of the above contributors was a shareholder in TIC.

[12] At all material times TSC Corp. was owned and controlled by the Respondent.

[13] The IFC scheme contemplated a lucrative rate of return. The shareholders of TIC received a monthly

payment of 3%. IFC paid monthly earnings from June to November 2006 at the rate of 10%.

[14] The difference between the monthly payments made by IFC to TIC and the distribution by TIC to its shareholders in 2006 was used by the Respondent to make payments to his company Bitter End for the use and benefit of CM and to reinvest the balance into IFC for the benefit of TIC. The payments to Bitter End during this period totaled $19,476 US.

[15] On November 1, 2006, the British Columbia Securities Commission (" BCSC") issued a Temporary Order and Notice of Hearing ordering, *inter alia*, all persons to cease trading in IFC investments (the " Cease Trade Order"). This order was periodically extended to October 2, 2007.

[16] The Cease Trade Order alleged that:

(a) the IFC scheme was a security;

(b) that IFC and the named respondents, PP, MS and DB were not registered to trade in securities and were promoting and selling the investment in violation of the *B.C. Securities Act*; and

(c) the MTN investment was fictional and fraudulent.

[17] The Respondent was aware of the Cease Trade Order and allegations on November 1, 2006.

[18] On December 4, 2006 the United States Security and Exchange Commission (" USSEC") commenced civil proceedings against IFC. Those proceedings alleged a ponzi scheme and IFC assets were frozen.

[19] The Respondent became aware of the USSEC action on December 6, 2006.

[20] The USSEC obtained final judgments for $25,000,000 US against PP and IFC in July, 2007.

[21] The Respondent did not advise all of the shareholders of TIC of the fraud allegations or the steps taken by the securities regulators.

[22] The Respondent admits this information was not disclosed to DF, HL and GG. The Respondent testified that JM and CM knew of the problems of IFC. JM denies this.

[23] The last monthly payment by IFC sent to the Respondent for TIC was on November 29, 2006. After a 3% distribution to the TIC shareholders on November 30, 2006 there remained $6,537.73 US of TIC's money in the Respondent's US trust account.

[24] TIC continued to make 3% monthly payments to TIC's shareholders between December 21, 2006 and June 25, 2007. The source of these funds was $2,537.73 US held in the Respondent's US trust account for TIC and loans to TIC from the Respondent's TSC Corp. Between December 10, 2006 and July 3, 2007 TSC Corp. contributed $29,259.96 US to TIC.

[25] JC was introduced to TIC as a new contributor and shareholder by JM. On April 11, 2007 JC contributed $47,700 US to TIC by means of a bank draft payable to the Respondent in trust.

[26] JC had no dealings with the Respondent prior to providing these funds.

[27] The JC contributions were used to pay out the shareholder, DF. JC testified that she didn't realize she would become a shareholder in TIC but that she believed that she was investing in the IFC scheme. However, she replaced DF as the seventh shareholder in TIC.

[28] The Respondent testified that he accepted JC's funds and agreed to her becoming a TIC shareholder on the basis of JM's guarantee of JC's position. JM denies any such guarantee.

[29] The Respondent did not personally ensure that JC knew about the fraud allegations and how her funds were going to be used. According to his own evidence, the Respondent relied on JM, an existing TIC shareholder, to do so.

[30] The Respondent deliberately chose not to deal directly with JC and not to disclose the IFC problem to her.

[31] The Respondent did not advise TIC that JC's funds should not be accepted.

[32] JC testified concerning her reliance on the Respondent and that, " he was the lawyer who took my money, so he is the person who is responsible for my money." She also testified that she knew the Respondent was a lawyer and " it made me comfortable knowing he was a lawyer; that I'm safe."

[33] As well, the documentation prepared by the Respondent that JC received before investing lent credibility and legitimacy to the IFC scheme.

[34] Despite the serious fraud allegations being made by the securities regulators, the Respondent's evidence was that he remained convinced that the IFC scheme was legitimate and TIC's investment was safe, at least until the summer of 2007.

[35] This confidence was based on representations by MS and PP, similar beliefs amongst other clients who invested in IFC that another British Columbia lawyer continued to send funds to IFC despite the BCSC Cease Trade Order and his understanding that MS and PP had approximately $40,000,000 US but that the US receiver had only seized approximately $10,000,000 US.

[36] The Panel finds that the Respondent's belief was sincere but unreasonable as it was based on representations and actions by parties who were highly involved either as managers or investors in the IFC scheme. There was no independent source of evidence to contradict the allegations of the securities regulators.

Analysis

[37] In a citation hearing, the onus of proof is on the Law Society on a balance of probabilities. " Evidence must be scrutinized with care" and " must always be sufficiently clear, convincing and cogent to satisfy the balance of probabilities test. But ... there is no objective standard to measure sufficiency." (*F.H. v McDougall*, 2008 SCC 53, 297 DLR (4th) 193.

[38] Section 38(4) of the *Legal Profession Act* sets out the various dispositions available to a hearing panel.

[39] The Law Society submits that the evidence supports a finding of professional misconduct.

[40] Professional misconduct is not defined in the *Legal Profession Act,* the Law Society Rules or the *Professional Conduct Handbook*. However, the case law as laid out in *Law Society of BC v. Hops*, [2000] LSDD No. 11 and evolved in *Law Society of BC v. Martin*, 2005 LSBC 16 characterizes the test as " whether the facts as made out disclose a marked departure from that conduct the Law Society expects of its members; if so, it is professional misconduct."

Allegation 1

[41] In determining whether the Respondent's conduct constitutes professional misconduct, the Panel must consider the professional obligations of a lawyer acting for a company used as a vehicle for investing pooled funds into a scheme once the lawyer becomes aware that securities regulators allege that the scheme is fraudulent.

[42] The Law Society submits that it is not necessary for the Panel to find that the IFC scheme was fraudulent or that the Respondent knew or ought to have known that it was fraudulent.

[43] Professional misconduct may be established in the absence of such findings on the basis that the allegations alone should have triggered certain obligations on the Respondent's part, *vis à vis* TIC and its shareholders.

[44] In *Law Society of BC v. Elias*, [1993] LSDD No. 182, the Benchers on Review held that:

> ... where the circumstances of a proposed transaction are such that a member should reasonably be suspicious that there are illegal activities involved under Canadian law or laws of other jurisdictions, it is professional misconduct to become involved until such time as inquiries have been made to satisfy the member on an objective test that the transaction is legitimate.

[45] In *Law Society of Upper Canada v. Tulk*, [1993] LSDD No. 115, it was held that:

> It is the submission of counsel to the Society that, by designing the transaction and acting as counsel to Orsini, Tulk provided a form of assistance to Orsini in a transaction which was abusive to the public. The design of the transaction, inasmuch as it eliminated the usual regulatory checks and restraints, became easy prey to a fraud. The public was left with no protection to the abusive conduct of Orsini. In designing this transaction, and in *ignoring incidents which should have raised suspicions,* Tulk became the tool or dupe of Orsini.
>
> (emphasis added)

[46] In submissions on penalty in *Tulk*, the Ontario Discipline Committee commented on the gravity of the misconduct and stated that " professional misconduct of this type, even where it is devoid of any fraud or misappropriation, is a serious matter and it is not to be condoned or treated lightly."

[47] In the present case, knowledge of the fraud allegations and other steps taken by the securities regulators should have raised the Respondent's suspicions, and he should have been alive to the possibility that:

1. the IFC scheme may have been fraudulent;
2. MS and/or PP, upon whose representations he relied, were complicit in the fraud; and
3. TIC's funds may have been at risk.

[48] As a logical extension of that suspicion, the Respondent had a professional obligation to advise TIC of the possibility that the IFC scheme was a fraud, that its funds might be at risk and to advise TIC to disclose this to all of its shareholders and not accept any further investment funds.

[49] The evidence before the Panel establishes that, even after he became aware of the allegations against IFC, the Respondent engaged in conduct that gave TIC's shareholders the impression that their investments were secure and continuing to generate earnings.

[50] This was done by loaning money from TSC Corp. so that TIC could make regular monthly payments to its shareholders after IFC was no longer in a position to make payments. Further, the Respondent did so without advising TIC's shareholders or advising TIC to notify its shareholders of the circumstances.

[51] The Panel finds those actions to be a marked departure from the conduct expected of a member and therefore professional misconduct.

[52] Lawyers have a positive obligation to ensure that they do not act in a manner that may have the effect of perpetuating a fraud on the public.

[53] This obligation is spoken to in the *Professional Conduct Handbook*, Chapter 4, Rule 6, which reads as follows:

> A lawyer must not engage in any activity that the lawyer knows or ought to know assists in or encourages any dishonesty, crime or fraud, including a fraudulent conveyance, preference or settlement.

[54] Similarly, the footnote to that Rule reads:

> A lawyer has a duty to be on guard against becoming the tool or dupe of an unscrupulous client or of persons associated with such a client and, in some circumstances, may have a duty to make inquiries. For example, a lawyer should make inquiries of a client who:
>
> (a) seeks the use of the lawyer's trust account without requiring any substantial legal services from the lawyer in connection with the trust matters, or
>
> (b) promises unrealistic returns on their investment to third parties who have placed money in trust with the lawyer or have been invited to do so.

[55] As well, the Respondent had an obligation to give full, proper legal advice to TIC and if TIC insisted on giving him instructions that were inconsistent with his professional responsibility, he should have ceased acting for TIC as required by the *Handbook*, Chapter 10 Rule 1(b).

[56] The Respondent was not at liberty to ignore his professional obligations simply because of TIC's instructions. That principle is drawn from *Law Society of Upper Canada v. Di Francesco*, [2003] LSDD No. 44. That panel held at paragraph 26 that:

> The member had an obligation not to allow himself to be a mere unquestioning instrument of his client's wishes ...

[57] The situation was exacerbated by the Respondent continuing to make monthly earnings payments to TIC shareholders without disclosing the source of those funds. The implied representation that the shareholders' investments were secure and generating revenue was obviously false.

[58] The above logic is supported by the decision of *Law Society of BC v. Bohun,* [2003] LSBC 8. In that case a lawyer allowed himself to be used to engender confidence amongst lenders in a fraudulent scheme.

[59] It should be noted that the continuation of monthly payments also had the real effect of hiding the dangers of the IFC scheme by removing the obvious warning of problems for other potential investors such as JC.

[60] Accordingly, the Panel finds that the Respondent's conduct was professional misconduct as it pertains to allegation 1(b) of the amended citation. With respect to allegation 1(a) the Panel does not find that the Respondent engaged in professional misconduct as alleged in that paragraph because the Law Society has failed to prove on a balance of probabilities that the Respondent owed any duty to inform those shareholders of TIC who were not his clients of the temporary Order and Notice of Hearing issued by the B.C. Securities Commission and/or the appointment of the receiver for IFC, which information was in the public domain in any event.

Allegation 2

[61] Lawyers have a duty to give a client undivided loyalty. Chapter 7, Rule 1 of the *Handbook* prohibits lawyers from performing any legal services for a client if:

> (a) the lawyer has a direct or indirect financial interest in the subject matter of the legal services, or
>
> (b) anyone, including a relative, partner, employer, employee, business associate or friend of the lawyer, has a direct or indirect financial interest that would reasonably be expected to affect the lawyer's professional judgment,

unless otherwise permitted by the *Handbook*.

[62] In his submissions, the Respondent admitted that he had breached the above *Handbook* rule, but he submitted that there was no conflict of interest as the interests of himself, TSC Corp. and TIC were identical.

[63] The Panel does not agree with that logic. The danger inherent in a conflict of interest is that the lawyer's professional judgment could reasonably be expected to be affected. This is certainly true in the case at hand.

[64] In *Law Society of BC v. Seifert*, 2009 LSBC 17 the panel held at para. [21] that:

> The Law Society does not want lawyers who are shareholders of the companies that they represent to be unclear about their roles and responsibilities as counsel. If a lawyer's financial interest in a client would reasonably be expected to affect his or her professional judgment, then it must be expected that the lawyer will withdraw as counsel.

[65] The panel in *Seifert* went on to add at para. [25]:

> A lawyer is often the last independent person standing between the investing public and the entrepreneurial promoters of publicly traded stocks. In these circumstances the public is entitled to nothing less than the utterly impartial review that independent oversight by a lawyer provides. The public trust requires that misconduct of this nature be treated with a severity that respects the importance that we feel is attendant upon the role played by the legal profession in this market place.

[66] The Panel has no difficulty finding that the Respondent placed himself in a clear conflict of interest, when TSC Corp., a company controlled by him, invested funds in IFC through TIC while the Respondent was acting for TIC. Furthermore, the Panel is satisfied that this is an obvious and dramatic marked departure from that conduct the Law Society expects of its members (*Martin*, *supra*) and finds that the Respondent engaged in professional misconduct concerning allegation 2.

Allegation 3

[67] JC testified that she was not aware of the IFC problems before she provided her investment funds. The Respondent takes the position that he told JM to ensure JC was made aware of the problems. JM denies this. However, even if the Respondent's evidence is preferred, the Panel finds that his conduct amounts to professional misconduct as he cannot discharge his professional responsibility by relying on JM.

[68] The Respondent should have returned the funds or, at the very least, personally ensured that JC was fully informed of the IFC problems. By accepting the funds and using them to pay out DF, the Respondent acted in a way that is a marked departure from what the Law Society expects.

[69] By deliberately choosing not to deal directly with JC, the Respondent abdicated his professional

responsibility.

[70] For the reasons stated above, the Panel finds that the Respondent acted contrary to his professional obligation to ensure that he did not act in a manner that has the potential of perpetuating a fraud on a member of the public. In addition, he failed in his obligation to give full and proper legal advice to TIC in respect of JC's investment.

[71] This finding of professional misconduct is supported by the decision of *Law Society of BC v. Grier*, [1998] L.S.D.D. No. 122. In that case, the respondent admitted and the hearing panel held that the respondent's conduct in placing investment funds with his client's mortgage brokerage company when he knew that the registrations of his client and his company were under suspension constituted professional misconduct.

[72] A lawyer's underlying duty is laid out in *Law Society of Upper Canada v. McKerrow*, [2002] L.S.D.D. No. 61. That panel wrote:

> The professional misconduct in this case is a serious matter. Lawyers who operate trust accounts undertake concomitant duties. They must be vigilant to ensure that they do not use their trust accounts to assist unscrupulous clients. They must exercise great caution and skepticism. It should be obvious to any lawyer that it is inappropriate to use his or her trust account as a means to facilitate transactions for a client whose own accounts have been frozen by the order of a court or tribunal. ...

[73] The Respondent relied on the decision of the Benchers on Review in *Law Society of BC v. Lawyer 10*, 2010 LSBC 02. That decision, at paragraphs [32] and [33] held:

> [32] A respondent must be culpable in order to have committed professional misconduct. The conduct must not only be a marked departure from the norm, but must also be blameworthy.
>
> [33] In order to determine whether the Applicant's (Respondent's) conduct is both a marked departure from the norm and blameworthy, one needs to consider precisely what it is that he did wrong.

[74] That circular logic makes each ruling dependent on its own facts. In the *Lawyer 10* case above, the respondent had relied on his partner and made an error in not adding that his statement was on information and belief in a supporting affidavit to an application of which his partner had carriage. It is distinguishable from the case before this Panel on its facts. In the within case, the Respondent had complete carriage of the matter and moreover, took active steps such as lending money and receiving JC's deposit, which the Panel finds to be blameworthy.

Decision

[75] The Panel finds that the Respondent has committed professional misconduct as alleged in allegations 1(b), 2 and 3 of the citation.