2012 LSBC 14
Report issued: May 03, 2012
Citation issued: September 8, 2009

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

Robert Collingwood Strother

Respondent

Corrected decision: Paragraph [33] of the decision was amended on May 9, 2012

Decision of the Hearing Panel on Applicability of Chapter 7, Rule 1(a) of the *Professional Conduct Handbook* in Allegation 1 of the Citation

Written submissions received: January 25, 2012, January 27, 2012 and February 1, 2012
Panel: Gavin Hume, QC, Chair, Gregory Petrisor, Alan Ross

Counsel for the Law Society: Henry Wood, QC
Counsel for the Respondent: Peter Gall, QC and Robert Grant

preliminary matters

[1] This is the second preliminary application at the request of the Respondent.

[2] The Respondent requests a ruling from this Panel relating to allegation 1 of the citation.

[3] As set out below, the Respondent is alleged to have taken a financial interest in a client in or around 1998. This Panel is asked to rule on the applicability of Chapter 7 Rule 1(a) of the *Professional Conduct Handbook* to the Respondent's conduct during that period. If we find that the scope of Chapter 7 Rule 1(a) did not contemplate the conduct alleged in the citation, then allegation 1 of the citation will be dismissed.

THE CITATION

[4] The Law Society issued a citation against the Respondent on September 8, 2009 and amended it on September 14, 2010. The citation contains two allegations, but only the following one is relevant to the issue in this application:

> 1. In or about, 1998, you breached Chapter 7, Rule 1(a) of the *Professional Conduct Handbook* and placed yourself in a conflict of interest with a client, M Corp. (Now [number] Canada Inc.) by taking a personal financial interest in a new client, S Corp., which was a potential commercial competitor of M Corp. in a business market involving tax shelters related to film production services.

CHAPTER 7 OF THE PROFESSIONAL CONDUCT HANDBOOK

[5] The applicable portions of Chapter 7 are reproduced below:

CHAPTER 7

CONFLICTS OF INTEREST BETWEEN LAWYER AND CLIENT

The purpose of this Chapter is to state the general principles that should guide a lawyer's conduct when the lawyer is invited to act both as legal advisor and business associate.

Generally speaking, a lawyer may act as legal advisor or as business associate, but not both.

These principles are not intended to preclude a lawyer from performing legal services on his or her own behalf. Lawyers should be aware, however, that acting in certain circumstances may cause them to be uninsured as a result of Exclusion 6 in the B.C. Lawyer's Compulsory Professional Liability Insurance Policy and similar provisions in other insurance policies

[amended 04/03]

Direct or indirect financial interest

1. Except as otherwise permitted by the Handbook, a lawyer must not perform 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, 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.

[amended 04/03]

[6] A footnote was added to Rule 1 in April, 2003. It states:

2. This rule does not prohibit a lawyer from acquiring an ownership interest in a client in lieu of a cash fee for providing legal services, provided the lawyer complies with Rules 2 and 5 of this Chapter.

[7] Although not specifically applicable to this discussion, Chapter 7, Rule 2 is discussed in the submissions of the parties. We reproduce it below:

Financial or membership interest in the client

2. A lawyer must not perform any legal services for a client with whom or in which the lawyer or anyone, including a relative, partner, employer, employee, business associate or friend of the lawyer, has a financial or membership interest that would reasonably be expected to affect the lawyer's professional judgement.

BACKGROUND FACTS

[8] We note that the parties have made submissions on this application regarding the presence of, absence of or conflict in evidence on certain points. We do not find it necessary to deal with any of the evidentiary points at this time. We have confined our discussion to the scope of the Rule and its application to the undisputed facts previously found in the litigation.

[9] The background to this disciplinary proceeding dates back to 1997. The majority of the factual background is set out in Reasons for Judgment issued by the Supreme Court of British Columbia (*3464920*

Canada Inc. v. Strother et al., 2002 BCSC 1179). That decision was appealed to the British Columbia Court of Appeal (2005 BCCA 35) and then the Supreme Court of Canada ([2007] 2 SCR 177, 2007 SCC 24).

[10] Based upon the findings from the above-mentioned Reasons for Judgment, the essential facts are:

1. Robert Strother was a partner at Davis & Co. and he provided tax advice to clients.

2. One of Mr. Strother's clients was M Corp. which was in the business of selling tax-assisted film financing products.

3. In or around 1996, to take effect at the end of 1997, the Government of Canada changed the rules relating to film financings and "closed the loophole" that had provided the business opportunity to M Corp.

4. In 1997 M Corp. had a broad retainer agreement with Davis & Co. Because M Corp.'s business closed down at the end of 1997, its retainer agreement with Davis & Co. was much more restricted in 1998.

5. A former employee of M Corp. (PD) approached Mr. Strother with an idea for a new business model for tax assisted film financing products.

6. PD incorporated a company to be the vehicle through which the new idea would be pursued (referred to as "S Corp." or "SH").

7. The exact origin of the concept that ultimately became successful is a matter of dispute. The Majority Decision of the Supreme Court of Canada states (with the names edited):

> 13 PD was able to put together enough of a scheme to convince Strother to draft a nine-page proposal that was submitted to Revenue Canada in March of 1998. Although the trial judge found as a fact that Strother honestly felt throughout 1997 and even after learning of PD's proposal that the TAPSF shelter was dead for good, Strother was obviously persuaded that PD's scheme was worth a try, and far from holding that opinion as a disinterested lawyer, he agreed to volunteer his services without charge to attempt to obtain the ruling, in exchange for a personal benefit. Strother later told his partners that he had an "option" to acquire up to 50 percent of the common shares of a new company called S Corp., a shelf company owned by PD, but in fact, on the evidence, he and PD had agreed in January 1998 that Strother would receive 55 percent of the first $2 million of profit should the tax ruling be granted and 50 percent thereafter. Out-of-pocket expenses for the ruling request were to be shared equally. Strother did not tell M Corp. about the possibility of a revival in the film production services business at any time.

8. As the matter would unfold, S Corp. did obtain a favourable tax ruling and Mr. Strother left Davis and went into business with PD.

THE ISSUES

[11] Chapter 7 Rule 1(a) generally prohibits a lawyer from both acting for, and taking a financial interest in, the same client. The questions for this application are:

1. Does Chapter 7, Rule 1(a) create an absolute prohibition against both acting for and taking a financial interest in, a client?

2. Does Chapter 7, Rule 1(a) provide protection to a client with whom the lawyer did not have a

direct financial interest? In this case, did the Rule protect M Corp. or only S Corp?

THE POSITION OF THE PARTIES

[12] The Respondent summarizes his position regarding Chapter 7 Rule 1(a) as follows:

> (a) first, the Rule applies only to the client for whom the work is performed and is intended to protect the interests of that client and not other clients of the lawyer. Accordingly, the Rule does not apply to protect M Corp. from any personal interest the Respondent had in S Corp. as alleged in the citation; and
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> (b) second, the client (in this case S Corp.) can waive the rule where the lawyer's financial interest arises from an ownership interest in the client in lieu of a cash fee for legal services, provided that the lawyer does not represent the client in the acquisition of his or her ownership interest and the client obtains independent legal advice regarding the acquisition.

[13] For the reasons set out below, we do not find it necessary to address the "waiver" issue raised by the Respondent.

[14] In further submissions, the Respondent states that wording of the citation does not support the Law Society's interpretation of the citation for the purpose of this hearing.

[15] The Law Society's position is as follows:

> (a) the fundamental allegation set out in allegation 1 of the citation is that, by taking a personal financial interest in S Corp., the Respondent:
>
> i. breached Chapter 7 Rule 1(a) and
>
> ii. placed himself in a conflict of interest with M Corp.
>
> (b) in 1998, Chapter 7 Rule 1(a) constituted an absolute prohibition against investment in a client;
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> (c) there is no language in the Rule that contemplates a "waiver" by a client in any circumstance;
>
> (d) The 2003 addition of footnote 2 (the Legal Fee exception) should not apply because:
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> i. it did not exist in 1998;
>
> ii. the Panel would require evidence of the timing and adequacy of the independent advice that PD received;
>
> iii. the Panel would need to assess whether the Respondent's interest would reasonably be expected to affect his professional judgment.

ISSUES TO BE DECIDED

[16] Our analysis of each question is set out below.

In 1998, did Chapter 7 Rule 1(a) create an "absolute prohibition" against a lawyer contracting with a client?

[17] We find that the answer to this question is "No".

[18] Our answer to this question is based on three elements related to the wording of the Rule.

[19] First, the wording of the preamble to the Rule does not support the view that the Rule itself was an absolute prohibition.

[20] The preamble states that “Generally speaking” a lawyer should act as either advisor or business associate, but not both. The use of the words “Generally speaking” indicates that the Rule was not meant to create an absolute prohibition. If the intention was to create an absolute prohibition then the drafters could have chosen not to include those two words. The sentence would have read: “A lawyer may act as a legal advisor or as business associate, but not both.” The meaning would have been clear.

[21] Second, the wording of Rule 1 itself also contains exceptions. The Rule begins: “Except as otherwise permitted by the *Handbook* …” If the Rule contemplates exceptions it cannot be said to be an absolute prohibition.

[22] Third, as noted above, the footnote to Rule 1 was added in 2003. It provides that lawyers are not prohibited from acquiring an ownership interest in lieu of a cash fee. Although that footnote was not added until 2003, we have no information as to whether the footnote enshrined the existing standard of conduct, or changed the scope of permitted conduct.

[23] Frankly, it is difficult to imagine that the Law Society considered that Chapter 7, Rule 1 created an “absolute prohibition” until 2003 but then decided to carve out a very large exception (taking an ownership interest in lieu of cash fees) and decided that the best method of conveying this significant change in policy was to place a footnote under Rule 1.

[24] Although this is an assumption on our part, it stands to reason that the footnote added in 2003 simply enshrined conduct that was already condoned (or at least not prohibited) by the Law Society prior to that date.

[25] Either way, for the purpose of this ruling, the footnote is simply another example of an exception to the Law Society’s suggested absolute prohibition.

[26] The Law Society also submits that we should not consider the footnote as having retroactive effect and that we should consider the Rule as it existed in 1998. We are not ruling on that issue. We note, however, that the footnote has been in effect now for nine years. We do not see that it would be in the public’s or the profession’s interest to make a ruling relating to this Respondent, based on conduct that is alleged to have been prohibited in 1998, but has been permitted since 2003.

[27] Based on this reasoning, we find that Chapter 7, Rule 1(a) does not constitute an absolute prohibition against taking a financial interest in a client.

[28] Even if Chapter 7, Rule 1(a) did not contain an absolute prohibition, the Law Society argues that the rule prohibited the Respondent’s conduct that is the subject matter of this complaint. The Law Society says that the Respondent was prohibited from taking a financial interest in S Corp. because it affected his judgment with respect to his representation of M Corp.

[29] This allegation leads us to consider the second issue.

Does Chapter 7, Rule 1(a) apply to protect the interests of other clients with whom the lawyer did not take a direct or indirect personal financial interest?

[30] The Law Society’s position on this point is that the Rule served to protect lawyers and the integrity of the profession by forbidding them from trespassing into potentially conflictual circumstances. This is a variation on the “absolute prohibition” argument. In other words, the Law Society says that, even if the Rule was not

an absolute prohibition, it still prohibited the conduct in which the Respondent engaged. Further, the Rule acts to protect other clients, like M Corp., in situations where the lawyer has taken a financial interest in a competing business.

[31] In his reply, the Respondent submits that the wording of the rule makes it clear that the party being protected, and therefore the party with a right to complain about the lawyer's conduct, is limited to the party for whom the legal work is performed (in this case S Corp.).

[32] The Respondent makes the following points:

> (a) Chapter 7, Rule 1 specifically prohibits a lawyer from performing "any legal services for a client if the lawyer has a … financial interest in the subject matter of the legal services." The Rule does not prohibit the lawyer from performing work for another client when the lawyer has a financial interest in the subject client.
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> (b) As noted above, the preamble to the Rule describes the scope of the Rule. It provides the "general principles" that should guide a lawyer's conduct "when the lawyer is invited to act both as legal advisor and business associate." The preamble does not discuss the lawyer's duties to other clients, only to the client who invites the lawyer to be both legal advisor and business associate.
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> (c) Further, as discussed above, the addition of the Footnote to Rule 1 in 2003 (ownership interest in lieu of a cash fee) does not contain any language that would guide a lawyer's conduct in respect of his or her obligations to other clients. It only discusses the client in whom the lawyer is taking an ownership interest.
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> (d) The Respondent also notes that this case appears to be a case of first instance. There are no prior cases where the Law Society has questioned a lawyer's conduct due to a complaint by a client where the lawyer did not take a financial interest in that client.

[33] We agree with the Respondent's position on this point. The wording of Chapter 7, Rule 1(a) does not contemplate the protection of other clients. As drafted, it is meant to protect the clientfor whom the work is performed.

[34] We note, in this respect, that the addition of the footnote to Rule 1 in 2003 specifically allowed for conduct akin to the Respondent's conduct herein, but does not anticipate the possibility that, by taking a financial interest in one client, the lawyer may be putting himself in a situation of conflict with another client. Frankly, we do not believe that the Respondent's situation was contemplated by the drafters of Rule 1. A plain reading of the Rule does not lead us to the conclusion that such situations were meant to be prohibited.

[35] As a result, we find that Chapter 7, Rule 1(a) creates an offence in certain circumstances where a lawyer takes a financial interest in a client and continues to act for that client. It does not create an offence in circumstances where the lawyer takes a financial interest in one client where that relationship may create a conflict of interest with another client.

[36] As a result, our answer to the second question is: "No". Chapter 7, Rule 1(a) does not apply to protect the interests of other clients with whom the lawyer did not take a direct or indirect personal financial interest.

SUMMARY

[37] Our findings above are sufficient to deal with this preliminary application. Allegation 1 of the citation cannot stand because:

(a) Chapter 7, Rule 1(a) does not contain an absolute prohibition;

(b) the opening words of allegation 1 restrict that allegation to the application of Chapter 7, Rule 1(a); and

(c) Chapter 7 Rule 1(a) is restricted to the client in which the lawyer has a financial interest.

[38] For the reasons set out above, we find that:

(a) Chapter 7, Rule 1(a) did not create an absolute prohibition against both acting for and taking a financial interest in a client.

(b) Chapter 7, Rule 1(a) did not act to protect other clients of the lawyer, only the one in which the lawyer took a financial interest.

[39] As a result, we dismiss allegation 1 of the citation.