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LAW SOCIETY of ALBERTA

Trust Conditions Guide

Introduction

The Law Society of Alberta Code of Conduct (the “Alberta Code”) was amended on November 1, 2011 to bring it into conformity with the Federation of Law Societies Model Guide. This made the Alberta Code accessible and familiar to Canadian lawyers practising across provincial boundaries under the National Mobility Agreement. And Alberta lawyers travelling outside the province were reassured that the rules are uniform across the country.

Prior to the amendment, the Alberta Code contained a familiar checklist or guide for working through trust conditions issues. It’s still a relevant and useful tool for decision making. The following Guide reflects the former Chapter 4, Rules 10 – 11, adapted for this online format.

The Alberta Code was amended in December of 2016 to make its numbering consistent with the Model Code to further facilitate lawyer mobility.

Guide

The following governs the use of trust conditions:

(a) An entrustor seeking to impose trust conditions on a lawyer must set forth each trust condition clearly, unambiguously and in writing. Trust conditions should state the time within which the conditions must be met.

(b) No trust condition imposed by the entrustor may be inconsistent with the terms of the clients' agreement.

(c) Subject to paragraph (b), the entrustor must not impose any trust condition that is impractical or manifestly unfair. This paragraph has particular application to trust conditions imposing time restraints or providing for the payment of penalty interest.

(d) The entrustor must clearly specify the subject matter of the trust (the "entrusted property") and must not subsequently purport to add to or vary the entrusted property without the express consent of the entrustee.

(e) If one or more of the trust conditions imposed on a lawyer is:

(i) unclear or ambiguous;

(ii) inconsistent with the terms of the clients' agreement; or

(iii) impractical or manifestly unfair,
or if that lawyer is unable or unwilling to honour one or more of the trust conditions for some other reason, then that lawyer must forthwith:

(A) return the entrusted property to the entrustor, or

(B) reach agreement with the entrustor to amend or clarify the trust conditions.

(f) If the parties agree on an amendment to or clarification of the trust conditions, the amendment or clarification should be confirmed in writing.

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(g) When a trust condition falling within subparagraph (e)(i), (ii) or (iii) above has not been amended or clarified by agreement within a reasonable time of the entrustee's receipt of the entrusted property, the entrustee must return the entrusted property to the entrustor.

(h) When a trust condition that the entrustee is unable or unwilling to honour for reasons other than those described in subparagraphs (e)(i), (ii) and (iii) above has not been amended by agreement within a reasonable time of the entrustee's receipt of the entrusted property, the entrustee must either:

(i) return the entrusted property to the entrustor, or

(ii) accept the trust conditions as originally stated by the entrustor.

(i) If a lawyer receives something which on a reasonable construction has been forwarded to the lawyer in trust, but which is not accompanied by express trust conditions, the lawyer must proceed in accordance with paragraphs (e), (f) and (g) above, which shall apply with the necessary changes in detail. Express trust wording may not always be used, particularly if the person forwarding the property is not a lawyer. The intention that the property be held in trust is often readily apparent nonetheless. If a lawyer believes that a trust was probably intended but is unsure, the lawyer has an obligation to contact the other party for clarification.

(j) No trust conditions may be added to, withdrawn or varied by the entrustor, whether or not they have been acted on by the entrustee, without the express consent of the entrustee. This paragraph prohibits the unilateral withdrawal or variation of trust conditions by an entrustor, whether or not they have been acted on by the entrustee. Although the entrustor must therefore seek consent to any change, the entrustee may have an obligation to agree pursuant to ethical rules dealing with reasonable request for time extensions or sharp practice (inappropriately taking advantage of another lawyer’s mistake).

(k) A lawyer who has agreed, expressly or impliedly, to trust conditions or amendments is bound by them, whether or not they have been recorded in writing as required by this rule, and whether the lawyer is dealing with another lawyer or with a third party.

Commentary

1. *General:*

The use of trust conditions is a mechanism that enables lawyers to implement a transaction agreed upon by their respective clients. If a transaction is jeopardized because the lawyers are unable to agree on trust conditions, the clients' opinion of those lawyers in particular and the profession in general will be adversely affected.

Trust conditions are also occasionally used by non-lawyers. In a particular transaction, the entrustor or the entrustee may not be a lawyer and will not, therefore, be subject to this Code. As a consequence, the enforceability of trust conditions purported to be imposed on a non-lawyer may be subject to question. On the other hand, a personal undertaking or trust condition accepted by a lawyer is binding on that person regardless of whether the other party involved is also a member of the legal profession.

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Failure of an entrustor to use the words "trust condition" or "in trust" does not relieve the entrustee from the obligation to perform if the action required of the entrustee is clear, and it is reasonable to construe the request for the action as a trust condition by virtue of the dealings between the parties or customary practice in the area.

A lawyer must also strictly and scrupulously fulfil any undertakings given and honour any trust conditions accepted by the lawyer in the course of litigation.

A lawyer must not implement instructions of a client that are contrary to professional ethics and must withdraw if the client persists in such instructions. A lawyer's ethical obligations override instructions given by a client to the contrary. For example, a lawyer cannot proceed on the basis of an arithmetical error made by opposing counsel. A lawyer must also tender cash to close a real estate transaction in accordance with trust conditions accepted by the lawyer, although the client instructs a holdback based on alleged deficiencies in the property.

2. *"Trust on a trust":*

Several paragraphs of the Guideaddress the alternatives available to an entrustee in dealing with the subject matter of the trust and the trust conditions imposed by the entrustor. An option not open to the entrustee is to attempt to impose trust conditions in turn on the entrustor. When a trust condition arrangement, or an undertaking or exchange of undertakings, has been established and all of the conditions or events giving rise to performance by the entrustee have been completed, the entrustee cannot escape or modify performance by adding a new term or by seeking to impose a new obligation on the entrustor. Rather, the entrustee must accept the trust conditions as stated by the entrustor, or seek amendment to those conditions in accordance with the Guide. If a client persists in instructions to impose a trust on a trust, the lawyer's duty is to withdraw after complying with the trust conditions earlier accepted by the lawyer.

Since an entrustee has no status or capacity to impose a trust on a trust (or “reverse trust”) despite the use of a phrase such as "in trust", "on the trust condition that" or "on your undertaking", the entrustor to whom such an attempt is directed may be entitled to ignore it, but has an obligation to so advise the entrustee. The imposition of a trust on a trust must be distinguished from the situation where an entrustor, concurrently with the imposition of trust conditions, undertakes to do something in connection with the transaction. This practice does not violate the Guide, and the undertaking is binding on the entrustor in accordance with its terms.

3. *Undertakings*

A lawyer must honour all undertakings given by the lawyer regardless of their form or the manner in which they have been communicated.

A lawyer's undertaking is any promise made by the lawyer (written, oral or implied) that is relied upon in some manner by another party. An undertaking is a matter of utmost good faith and must be personally fulfilled by the lawyer giving it, whether or not the recipient of the undertaking is another lawyer. Failure to use the word "undertaking" does not relieve a lawyer of this responsibility when the intention of the parties is clear.

Occasionally a client may covenant to do something through counsel. This situation warrants some care on the part of the lawyer since, unless it is made manifestly clear that the client's covenant is not a personal undertaking of the lawyer, responsibility for performance may be attributed to the lawyer.

When retained in a matter involving the performance of undertakings or trust conditions, a lawyer should fully explain to the client at the outset the implications of a lawyer's undertaking or acceptance of a trust condition and the fact that, having given an undertaking or accepted a trust condition, the lawyer cannot accept later instructions not to perform.

History and Enforcement of Undertakings

The unique employment of trust conditions in western Torrens jurisdictions is discussed by Justice Coté in the ***Carling Development Inc. V. Aurora River Tower Inc.*** *[2005] A.J. No. 988* at para. 28 – 36. The appeal judge comments that there is "a lamentable dearth of authority on the nature of solicitors' trust conditions." Probably, it is in fact commendable that there are so few reported cases – an indication that Alberta lawyers recognize and respect trust conditions for the valuable tool they are.

Modern standards respecting the enforcement of trust conditions were established by Justice D.C. McDonald in ***Witten v. Leung***, [1983] A.J. No. 883. While finding no need to enquire into the propriety of the trust condition at issue, the court said, "…there being no doubt as to the clarity of the trust conditions, the obligation of the receiving solicitors to comply with them was absolute" (at para. 18). Moreover, the duty to comply with undertakings prevails over the contrary instructions of the client. The court held that the "…obligation of the recipient solicitors to respect and observe trust conditions upon which documents are received from other solicitors cannot be shackled by instructions given to the recipient solicitors by their client". (para. 6). That the subject trust conditions complied with the underlying agreement and were capable of being fulfilled was self-evident and unchallenged. The court found it unnecessary to consider whether trust conditions were different from undertakings but did find that the judicial enforcement of each should be the same. Despite the absence of precedent authority, the court endorsed enforcement of undertakings and trust conditions by summary procedure.

A few years later, the Manitoba Court of Queen's Bench, following *Witten*, confirmed that summary proceedings brought by Originating Notice of Motion between the solicitors directly was the appropriate method for enforcing trust conditions and undertakings: ***Regatta Investments Ltd. V Haig***, [1985] M.J. No. 413. The Alberta Court of Appeal also affirmed that action to enforce trust conditions is properly brought by way of Originating Notice of Motion: ***Minsos, McLeod v Wedekind***, [1988] A.J. No. 447. Funds had been sent in trust for the delivery of a share certificate but were disbursed by the receiving law firm. The firm had been unable to obtain the release of the certificate from hypothecation to a bank. It was recovered by the date of the application and the court ordered delivery by a specified date "on pain of contempt".

Former Law Society of Alberta Practice Advisor Barry Vogel QC often discussed trust conditions in his column, *Ethically Speaking*. In the June 1999 edition, he reviewed the imposition of trust conditions by and upon non-lawyers. Certainly any person can impose a trust condition upon a lawyer and lawyers are bound to recognize circumstances that give rise to trust conditions, even when the magic words are not employed. However, a lawyer cannot expect unequivocal and absolute compliance with a trust condition imposed upon a non-lawyer. A lawyer reckless enough to impose a trust condition on a lay person creates nothing more than a contractual obligation, at best. Trust conditions between lawyers are enforceable in equity as fiduciary duties outside of the contractual obligations between the respective clients.

There is indeed a dearth of authority in Canada respecting attempts to enforce improper or impossible trust conditions. Lawyers in Alberta tend to recognize the impropriety of a trust condition that depends upon performance of an action by a third party or the happening of an

event beyond the lawyer's control. There are some instances in the annals of Law Society discipline, discussed below. In the English case of ***Udall v Capri Lighting*** (1987), 1 Q.B. 907 a lawyer foolishly or recklessly undertook in the course of litigation that his clients, the defendants, would provide security for the claim. Enforcement of the undertaking was sought when the defendants failed to post the security. On application, the Court ordered the lawyer to carry out the undertaking. The appeal court, however, recognized the futility of doing that and remitted the case to determine whether the lawyer should pay compensation by way of damages, if in fact there had been a loss.

In ***Carling Development V. Aurora River***, the Court, however, challenged the earlier notion that trust conditions in Alberta equate with solicitor's undertakings in all cases. Probably, McDonald J. in *Witten* only made the comparison in respect of the issue of the enforcement of trust conditions or undertakings, having no need to draw the theoretical distinction. Trust conditions may be, according to *Carling*, something more than undertakings. A lawyer may, for instance, undertake to have lunch with another lawyer next week.

Undertakings and escrow agreements do not solve all of the problems of giving possession before the transfer of title in a Torrens jurisdiction. The judgment concludes that "trust conditions between solicitors are intended to create, and do create, a traditional trust". (para. 47).

Justice Coté notes the following:

- Trust conditions which are imposed and accepted have all the necessary elements of express trusts in that the lawyer holds the property for other persons or purposes and not beneficially, the trust property is clearly identified and the beneficiaries are certain or ascertainable.
- A mere undertaking may not always bind the lawyer's client.
- Trust conditions are enforceable as trusts notwithstanding the equities between the respective clients or their contradictory instructions.
- "If something goes wrong, proprietary remedies are available, not merely an unsecured claim for money compensation. If the recipient's client or some non-lawyer gets possession of the documents or money entrusted, he and they are just as bound".
- Trust conditions are imposed by others; undertakings are given.
- Trust conditions are linked directly to the use of documents or other acts and do not depend upon a lawyer's assent.
- To use a document received in trust is to accept trust conditions; a lawyer must accept conditions or reject them and return the trust property.
- Any variation or waiver of a trust condition made orally should be confirmed in writing.

The Alberta practice of relying upon lawyer's trust conditions is confirmed and strengthened by this judgment. However, the Court goes on to discuss the propriety of trust conditions (para. 58 – 63): The objective of employing trust conditions between lawyers is to facilitate the agreement between their clients. It is inappropriate to attempt to re-write the deal using trust conditions. Similarly, trust conditions calling for performance by third parties of acts beyond the control of the receiving lawyer need to be carefully considered.

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> …it is easy to mix together two topics which should be kept distinct one topic is when it is proper to impose a certain trust condition. The other topic is the effect of using documents after such a condition is imposed (properly or improperly).
>
> If a party has his solicitor impose a trust condition which is inconsistent with the existing sale contract that may be a breach of the contract. And if a solicitor imposes a trust condition inconsistent with an existing binding sale contract, that may also be professional misconduct. But the recipient has a cheap easy solution. He or she should at once refuse in writing to accept the trust condition. At the same time, he or she should either get an acceptable written variation of the trust condition, or return the entrusted documents unused.

Law Society Discipline

The area of real estate gives rise to may calls to various departments within the Law Society of Alberta and the Alberta Lawyers Indemnity Association ("ALIA"). The Law Society encounters a significant number of concerns regarding real estate transactions as well as common concerns relate to breaches of undertakings and conflicts of interest. Trust condition issues also commonly arise in commercial transactions and the settlement of litigation.

Family law practitioners are strongly urged to use independent third party lawyers to represent the parties in the sale of the matrimonial home or other property. It is an inherent conflict of interest to attempt to represent both spouses in the house deal while under instructions in the family law matter. This frequently leads to problems in connection with the disposition of the proceeds.

Naturally, the Law Society has some persuasive power or can play a mediating role in resolving inter-lawyer disputes respecting trust conditions.

Some examples from Law Society of Alberta conduct proceedings include:

- A lawyer was reprimanded, with costs, for paying out trust funds to his client, relying upon the client to bring in discharges of encumbrances later.
- A lawyer was reprimanded and fined, with costs, for imposing trust conditions that were inconsistent with the terms of the contract between the parties. The same member was also found guilty of failing to agree to reasonable requests to amend his trust conditions.
- Another lawyer was reprimanded, with costs, when funds were not returned within the conditional thirty days and, more than a year later; the deal had still not come together.
- A lawyer was reprimanded, with costs, for misrepresenting to another lawyer that he held in trust the amount of the GST on a transaction.
- Having undertaken to do something beyond his direct control, a lawyer was reprimanded, with costs, and referred to practice review, for failing to honour an undertaking to another member within a reasonable time (9 years), and failing to respond to the Law Society.
- Another lawyer was reprimanded, with costs, for failing to honour an undertaking to discharge an encumbrance when he was " hopeful", rather than certain that he would be able to clear title.

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Other lawyers have been sanctioned for accepting the contrary instructions of the client in paying funds out, wrongfully assuming that an amendment had been agreed, using documents on the assumption that an unusual trust condition did not need to be amended, or refusing to honour an undertaking because the amount of a holdback was considered to be trifling.

There are numerous other more or less egregious breaches and failings by lawyers in the area of trust conditions. A common theme begins to emerge. Except for cases of outright misappropriation from trust accounts, the lawyers involved in virtually all of the cases were striving to serve their clients, diligently, zealously, faithfully. It is ironic that unethical behavior should be motivated by an otherwise lofty sense of duty to the client. The reality is that clients are in fact poorly served by a profession that would be willing to compromise high ethical standards.

The Law Society has sanctioned an Alberta lawyer in respect of attempting to impose trust conditions that were inconsistent with the underlying client agreement and in refusing to make reasonable amendments.

Practice Advisor Mediation

Where lawyers have disputes concerning trust conditions, they may agree to informal mediation with the Practice Advisors. Both lawyers must agree to the non-binding process. However, conference call discussions with the Practice Advisors do not require the filing of applications or affidavits, or any documents at all, and can be arranged at a moment’s notice.